Fortune Brands Innovations, Inc.
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Fireside Chat Transcript

FBIN Participants

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Collin Verron: Good afternoon, everyone. Thank you for attending the Deutsche Bank Industrial Conference. I am excited to have Fortune Brands management team here. Jesse Singh, the CEO, Dave Barry, the COO, and Ashley George, the interim CFO, with us today. So I guess I'll just jump right in. And if there's questions in the room, please feel free to raise your hand, and we'll start peppering those in as well. So I'm just starting a lot of news bad fortune over the past couple of months. Jesse, you had your first earnings call with Fortune Brands. I guess I just want to start on the strategic refocusing here. You called out the organization had become too internally focused. There's some corporate complexity that kind of pulled attention away from customers. I guess what are the most important structural or behavioral changes you guys are looking to make to sort of reorient Fortune Brands around service, product innovation, customer responsiveness?

Jesse Singh: Yeah, thanks for the question and thanks for having me here. You know, as you pointed out, it's been about six weeks that I've been on the job. You know, I came into the role, you know, very excited about the opportunity of having really, really strong brands that have, you know, really good potential and you know, coming in, you know, it's pretty obvious that that opportunity exists. In a pretty meaningful way for the long-term in particular. I think, you know, as you pointed out, I highlighted a few things on the earnings call. I think number one, we've had a lot of change in the organization. You know, we've obviously had some turnover in management, you know, starting at the top. We, you had some activity at a board level. But we also made some changes relative to how we're organized and our headquarters consolidation. And all that's led to a lot of internal discussions in the company and a focus on, perhaps at times, the wrong things for the right reasons, which is how we operate. I think we're trying to refocus the company back to just our great brands and our great customers, and really being focused externally. And as part of that, we can better align our organization to operate in a way that's more focused on the customer and more focused on enabling our businesses to deliver against our customers, deliver it in a more profitable way, and also do it in more streamlined and responsive way.

Collin Verron: I guess just product innovation came up a few times on the earnings call. Can you just touch a little bit about sort of where you guys were in product innovation, sort of the guideline or the hope of where are you going to get that to and sort of the pathway to get there?

Jesse Singh: Yeah, I think first we've got to be oriented on the right customers and the right customer segments and we've got a lot of opportunity. There's areas where we've good penetration. There's area where we're under-penetrated and product development is pretty straightforward or innovation can be pretty straightforward which is you need the right pipeline of opportunities. You need to understand where you have the right to win. You need to understand your internal capabilities. And then you need to make sure that you have the right processes to deliver against it. You know, coming in, over the last couple years, we've probably under-indexed in terms of new product launches. I think with Dave at the helm over the last almost six months, we've been really focused on making sure that we restart our pipelines. I think in each of our businesses we've got a pretty good list of potential new products and things that are in flight. I think if you look objectively, I would say that there's opportunities to really speed up how fast we bring products to market and then when we bring new products to market, just really making sure that we do it in the right way and the most impactful way. So I think coming in as you look at obviously innovation is in our name, there's a lot of opportunity for that. I think part of the realignment against businesses is just making sure that we launch more products that are relevant to our customers and do it a bigger way.

Collin Verron: It's a great pivot to my next question just around the commentary on decentralizing your capabilities. I guess as you move the brand marketing and advertising resources back into the business units, I guess what changes do you expect your customers or channel partners to actually feel, and I guess how quickly, how quick of a process is doing something like that?

Jesse Singh: Well, first, as you pointed out, we've taken steps to realign against, realign- we've actually moved marketing back into the businesses. We had gone through, you know, a phase where we thought a more centralized organization in marketing would be, you know, give us more scale and leverage. I think what we found in that centralization is we made it more complex. We became a bit slower. And we were less responsive to the opportunities. And so, you know, as we've realigned that back in the business, it should give us an opportunity to just be more responsive and execute in each of our businesses in a bigger way. And I think it's going to be similar. We already talked about the new product side of things. I think it'll be similar in terms of our ability to execute on new products, and I'll just give you a tangible example, like why do I think it's going to be faster?

We've got a terrific Yale Locks business, right? It's an interconnected lock business. It's one of our smaller businesses, but I think its got, you know, good potential. To get some of the products through development would have required five separate organizations to be involved in just moving a new product through the organization. These are five separate functions within R&D. Then you add to that, you would have had a separate marketing function, you've got a separate supply chain function, you may have had a separate PR function, you may have a separate digital function. So you think about the complexity of trying to execute a new-product launch. You know, that consolidation back towards and aligned against the businesses should really give us a lot of speed. So the outcome to a customer should be better responsiveness, better service, and, you know, better engagement, especially from the channel side, for more growth.

Collin Verron: I guess on the timeline to do a lot of these things, I think on the call you mentioned by year-end you expect the businesses to be realigning against these new priorities. I guess what are two or three milestones investors should be watching for, whether that's service levels, new product launches, cost savings, like to gauge whether the reset is working and on track, kind of sort of that timeline.

Jesse Singh: Yeah, I would say we're early days in terms of, you know, specifics, and I know it can be frustrating. We all want tangible things we can point to that are quantifiable. I would say from a, you think about what we talked about on the earnings call, some specifics. I think number one, when you think about our service levels, as we talked about, and I know you may have a question later on that, but as you think of our service levels, they have not been to the level that they should be. We are making changes, in particular on our water business, to some of our processes, to make sure that we get back to the service levels that our customers expect and deserve. We would expect a lot of those changes- we would expect a lot of our service levels to come back to normal by the end of the year. And then we should continue to see improvement beyond that, as we move into next year. Now, we're incurring some, you know, premium air freight to get there. We may have some incremental inventory that we need to carry to deliver that. That will probably – hopefully the air freight won't carry into next year, but we may have some excess inventory that we need to carry as we work our way to improving the process. I think we've talked about cost down in the organization. I think Dave at the last earnings call, last two earnings calls has talked about a $70 million cost takeout. We should expect all of that to be effectively done by the end of the year. And in terms of the impact to the business, from a cost and margin standpoint, we're balancing, realigning, taking some cost out but yet reinvesting in our businesses for the long-term. When that balance works out so that the net of that is accretive margins, I think remains to be seen. And we'll, you know, as soon as we get a better sense of that, we'll talk about it. But right now, you should think that in parallel, we're trimming some costs and expanding others as part of that realignment. Dave, I don't know if you have any other comments on top of that?

Collin Verron: And I guess just maybe diving a little bit into that, I mean, on the updated EPS guide applied roughly 30 cents of pressure, I think, from all the actions that you guys are doing, 20 cents from the investments, 10% from that service level constraint. I guess, how should the investment community look at it as like temporary catch-up spending versus maybe a more permanent step change because of like all the product innovation you're investing in or something like that?

Dave Barry: Yeah, I'll start on that one, Collin. I think we just first characterize the commercial environment, the operating environment. It's very consistent from last quarter when we reset guidance. And what we're trying to give us some room for, one, is just around our execution on the service side. And so the 10 cents of volume that we called out is really our inability to go chase new business while we're having trouble fulfilling our existing business with our customers. And so we're pulling back on some areas that we probably would have leaned into in the second half until we can get our service right. The 20 cents, I'd think of it in three buckets, and I can talk a bit in more detail about each three. So one is service-related investments. The second, I would say new product development and commercialization associated with that.

And the third, some upper funnel brand-building and marketing behind some of our new campaigns.

On the service investment, what we're really trying to do is service our customers at their expectations while we're rebuilding our sales and operations process underneath. So as we went through headquarters transition, the team that we had left sooner than expected and we had to rebuild that team. And at the same time, we're rebuilding the process back to where it was when it was working prior. To compound things, we turned on a new system for Moen to plan that wasn't working. So you had a new team, a new system, in the process of unwinding that system, getting the team up to speed and bringing some talent back that we let go to help accelerate that. So think of it as rebuilding the process underneath while investing on top of that on air freight, on distribution costs like overtime, looking at some different supplier configurations that may be higher cost but better service for a period of time just to make sure we're delivering on our customer commitments. You know, I would expect as we move into early next year that a lot of that overlaid investment starts to tail off as the underlying process comes up and is more mature. But as you know, these things, they take a few cycles to run through, especially when you're talking about a complex, long lead time supply chain.

You know, new product development commercialization, Jesse touched on that. How do we get the right things to market faster? How do work with our suppliers to pull things off the shelf? Get them into market faster? And then how are we commercializing them with excellence once they're on the shelf to pull them through? And then the final bucket on the marketing piece, we launched a Moen, a new Moen marketing campaign for the first time in a handful of years last quarter. Master Lock has a new campaign that we launched last year that's performing. And so how are continuing to seed that upper funnel investment to drive awareness? I'd say both of those, it's probably a near-term acceleration of investment that then you know, either gets to a steady state or even, you know, pairs back some as the organization starts to mature and the process starts to work a little bit better. Underneath these investments though, we're pulling costs out of the business, and Jesse alluded to that as well, and you know where we have excess corporate costs, where we have resources that aren't aligned as closely with the business as they need to be, we are working on some of those structure items in the near term.

Collin Verron: Really helpful color and I guess just following up maybe on the upper funnel investments I guess is there particular businesses that you feel like require more attention than others or is it going to be pretty proportional to like the size of each business now? I guess like how should we think about sort of where you think maybe you under invested in either product innovation or

Dave Barry: My view is it's relatively proportional to the size of the business. I mentioned we have new campaigns in Moen and Master Lock. I think there's more we can do with Yale and there's more we could do with Therma-Tru and Larson. It might look a little bit different than upper funnel investment, but still investment to drive the brand, but relatively proportional.

Collin Verron: Okay, and I guess just pivoting maybe to the service and you alluded to some of the operational side of things. And you talked about this a bit on the call, but I guess when you're talking about reverting processes that have historically worked better, what exactly has to be reset and how long does it take to be reset and then sort of what gives you confidence that those service levels can return to baseline of maybe not creating the excess inventory for a long period of time.

Dave Barry: Yeah, I'm glad you mentioned inventory because we've taken constraints off of inventory for the near term while we work on service. You can expect our inventory to be a bit higher in the near term. We do believe there's a medium to long term benefit in inventory, but we need the process to work before we can get after that. We know how to do this. Actually, I've been in the business a long time, Jesse's been in businesses where this works. It is all the way from demand planning through to delivering to the customer. It's rebuilding that process with the right talent. Some of it new, some of it we've had in the past that we're bringing back that we lost through the headquarters transition. But we've executed on this in the past. So it's something that is very fixable and we know how to do it. It's just having it time, because the supply chain is six to eight weeks, if not longer, in some cases. And so you have to get the right forecasting inputs. You have to send the right signals to the supplier. You have look at the right data. And then pull it all the way through the DCs to the customer. And so at each step along that process, there were breakdowns that we're fixing. That's all. I don't know if you've got anything here?

Jesse Singh: Yeah, and as I mentioned earlier, and I think Dave's touched upon it, you know, I think we'll be in a different place, you know, as we move through the end of the year. And I think part of, you know, what we're recognizing is, you know, we want to be a really good- we want to make sure that we're a high-quality, high-service company which we have been for many, many years. And we've had a short-term variance against that. We'll get it back, but we're going to be thoughtful about not over-promoting or doing something that's going to create excess stress on the system, and we're doing this for the long term. We're not here to try to ship a bunch of product out in one quarter or the other to try to hit a number, we're going to do what's right for the long-term health of the business and for the long-term health of our customers. I think that's an important overlay here, which is part of why you've seen a bit of the variation on the guidance and all that. We just want to make sure that this is a fantastic business that's got enormous upside in multiple market segments. I mean, there's a lot of spaces where we have the right to compete in, and we want to make sure that we're doing things in a really thoughtful, measured way that leads to long-term value creation.

Collin Verron: So I guess following up really quickly on the right to win. I mean, is there a segment particularly, whether that be channel or end market specific, where you think that's been under-penetrated at Fortune going past recently- in the recent past?

Jesse Singh: Look, I wouldn't be a growth person if I didn't think there were multiple areas of under-penetration. I would say that if you just look at, numerically, if you look at the, if you look, for example, at the Moen business and the Therma-Tru business, we've had a really good business tied to single-family new construction. That's a great business to be in, you know, always. It happens to be a business that's under pressure right now. So the general theme I would give on the company is that we need to continue to expand in repair and remodel, which tends to be a larger, more complex, more fragmented part of the market. And within there, there's a number of subsegments where we think that we have the right brand, we have the right products and we have the right to play to use your- to use your question. And so we're going to be very selective about targeting some of those areas where we believe in general the R&R, we're underpenetrated, we'll be select on targeting some those areas and investing against that and in all of our businesses.

Collin Verron: Great color. And I guess going back to the S&O piece as to really quickly, you mentioned reverting and turning off a newer piece. Is there going to be an additional layer of investments maybe in the future as you sort of modernize that process? Is there a next level that you guys need to be taking? And what's the timing? How does that play out in the feature?

Dave Barry: Yeah, I mean, in my view, not a material investment, right? It's really getting back to the basics. We have functioning ERP systems where a lot of this work takes place and just getting people trained up and understanding how the business works in those systems is really important. I think where we got into some trouble is we tried to make these overlays on top of the core systems and use what appeared to be newer, better tools, and it didn't work, right, the implementations didn't' work, and so trying to unwind some of that. You know, I also think it's interesting with AI, I think all of these systems implementations look different in the future than they have, and that world is changing rapidly. So you don't want to start down a path of a significant implementation, knowing it could look very different, even six to nine to 12 months from now.

Collin Verron: Is there any questions in the room sort of around the investments or anything like that?

Unidentified Audience Member: [inaudible]

Jesse Singh: The concept of reinvestment is to make the business stronger, to make our customers stronger, and to create more value. In my generic view of business, lowering price is not creating more value, it's just- it's a transactional move. I also fundamentally believe that we're in a market where people choose the right product for what they need and you've got to have value in what you sell. But we sell faucets, what's our like ten thousand dollars? We've got faucets in the multiple thousands of dollars and we have faucets that might be you know, a hundred, right, and in each case we've got a deliver the right value there. I'm not a big "let's make a deal" sort of a person. I am not going to say that there is not going to be appropriate actions along the way, but I think fundamentally when we are building this business, it's really about investing for value creation, for both ourselves and our customers.

Unidentified Audience Member: And then is there a portfolio review process you're going through?

Jesse Singh: I think the way- so if you, and the question by the way for those that may not hear it is there a review process on the portfolio beyond Fiberon? I would say at a macro level, if you look at our portfolio, between our three kind of core pillars and then our two what I've defined as adjacencies, which is our two interconnect businesses, we feel really good about that in general. Now within each of those, are there areas where we might need to de-invest, put on hold, deal with an operational issue or deal with a geographic issue or optimize? We'll absolutely look at that. But not at a corporate level.

Collin Verron: I guess maybe pivoting to the $70 million savings, cost saving program that you guys have in progress, I guess any colors to like where the most meaningful savings are coming from and does the broader simplification work suggest the opportunity could ultimately be larger than just the 70 million that you guys are calling out, and I guess just helping investors think about sort of the potential around that?

Dave Barry: Yeah, you know, I'm happy to start and Jesse, add color. I think if you start and look outside in, the peer data and the benchmarking data would indicate there's a bigger opportunity than the 70 million. I think we have to be thoughtful around how we do that, when we do that, how we sequence it with investments that need to be made to get the business set up for success in '27. But I think about the effort broadly as when we changed our structure, we created, I'd say, over time, an outsized corporate piece and outsized centers supporting the business that both need to be, you know, taken down. One, the corporate, like, reduce the corporate expense, and this isn't all people cost, right? There's indirect spend. You know, we have two buildings as soon as Jesse started. We looked at our head count. We're going to go down to one building, right? That's, there's opportunity to reduce footprint, get indirect SG&A out. And then I think of it as moving the people who are in these centers back closer to the business. The one we talked about earlier that we executed last quarter was our marketing and our insights organization. And as we did that, there are actually efficiencies that come out of it because you can align the resources more closely to what individual businesses need and they're not in a center trying to fulfill everyone's needs. And so I think that's the genesis behind the 70 and we'll continue to work through it, but I just think of it as reducing that corporate structure to some extent.

Jesse Singh: I think longer term, I think we recognize that our SG&A as a percent to sales over a period of time has creeped up meaningfully. And you could argue what are the causes. We obviously spun a business out. There's all sorts of ways you can look at it. I think that over the long term, and you're going to ask, what's the timetable on a long term? But as we move through '27 and to '28, I think as we realign things, which might take some incremental investment, I think as we start to move through when the realignment's done and we've settled into our new business operating model, that we should definitely see SG&A leverage. I think, you know, part of my long-term view of our equation is that we should be able to operate in a more efficient way, and in an ongoingly efficient way from an SG&A standpoint.

Collin Verron: Okay, I guess moving over to inflation and maybe price cost and this might dovetail to one of the earlier questions around pricing. I mean, you guys increased the guide a little bit for the increased commodity cost. I think it was like a 10 million dollar lift. You called up the metals being the primary driver. I mean, I guess given the service disruptions, how confident are you in Fortune Brand's pricing power to really offset sort of these rising inputs if Inflations continues to accelerate as you look out into '27 and '28.

Ashley George: Yeah, yeah, I'm happy to talk about '26 price cost dynamics if it's helpful I'd say in general. It's probably too early to start talking about '27 at this point You know we'll continue to focus on talking about our '26 execution And we'll come back probably a little bit later and talk about '27

Collin Verron: And I guess like on '26, the pricing in the back half is probably is tracking in line, even though with the service disruptions, I guess, how would you frame the conversation around that?

Ashley George: Yes, if I look at '26 dynamics, pricing at low single digits, and that's pretty consistent all year, and then as you look at the combination of tariffs and inflation, that price-cost equation turns to favorable in Q4, and that is primarily driven by the year-over-year compound tariffs being favorable by the time we get to Q4.

Dave Barry: As you think about the guide, one of the questions we've had from people is that you still have a bit of a margin step up in Q4 that looks unusual based on your typical seasonality. There's 200 basis points of favorable price-cost, the price is in the market, the cost is on the balance sheet. There's a really good line of sight to that. Some of the cost-out activities start to accelerate as you get to the fourth quarter, and then we're making some investments to offset that. And so the top line, it's not top line-driven. We're not betting on a market recovery or a big volume lift in the fourth quarter. It's purely what we're seeing in the market from a price standpoint, what's on the balance sheet, offset by some investments.

Collin Verron: I guess maybe longer term than in water. I mean that business is historically been super strong margins, right? Like at points mid 20 percent EBITDA margins Has the long-term margin in that business changed in your mind as you invest in things like as you accelerate your product innovation or do the top of the funnel marketing that you called out or your supply chain or is it still really that level of profitability for that business longer term?

Jesse Singh: Yeah, I think step one, as we think about profitability, we've got to look at profitability of the enterprise. And as we talked about, as I just mentioned earlier, I think that we should have an opportunity to get better SG&A leverage across the enterprise, which should allow us to reinvest and we'll get that leverage even with reinvestment over the long term. But that should give us an opportunity to continue to invest in the businesses. And then, you know, specific to water, so I think that's the kind of the macro theme, independent, I don't know that we're going to be specifics on what's going to happen in each business unit. I think water is a really good business where we have, you know, a differentiated product, and we just view it as a good market. And so what's the right balance of what our margin structure should be, given both our premium portfolio and our Moen portfolio? I think we'll communicate that more as we kind of go through the cycle. So I would say we're ready to communicate a bit at the macro. I think we've got a, you know, we- we've got to give a better indication in the future of just that blended mix. But there are actions we can take that are really independent of the market. Think about improving our operational execution that we think will be beneficial to that margin equation. I mean, not just the short term, not just the lapping the service issues and all that, that's certainly part of it. Think about the inefficiency we've incurred. Those are all positive things, but there's also some tweaks we can make. There's parts of our portfolio that are, I mean, we make a lot of products in there. There's parts of the portfolio that are remarkably unprofitable, that we have an opportunity to address.

Dave Barry: And I think what I'd add maybe just to contextualize the very near-term margins, like what you saw in the quarter for water, there's 380 basis points of price-cost on favorability and 200 basis points of incremental cost to serve, right? To have a 580 basis point, almost 600 basis point headwind, price-cost will start to ease as we move into the first part of next year, through the fourth quarter of this year. We would expect cost to serve as well, as I talked about, we ramp up that process, starts to ease. So then you get to the discussion, Jesse laid out is what's the right kind of medium to long-term margin based on our growth ambitions and our level of investment.

Collin Verron: So, again, this question was sort of answered earlier, but I guess to be curious is to like, it sounds like you view the security business and the outdoor businesses as being core part of those three pillars I think you mentioned. I guess what makes those business core in your view to Fortune as we look to kind of understand the strategy of kind of having those as parts of, I guess, the core for lack of a better term?

Jesse Singh: Yeah, I think your question is really around what is Fortune and what constitutes what the company is? And obviously, over a 20-year, a multi-decade period, I just ran into someone on the way in who I chatted with briefly and he said, "Well, I guess I should chat with you about golf balls." So I'm like, yeah, that was a different iteration. A fortune. It wouldn't be bad right now, but it still wouldn't fix my golf game. I think our focus right now is each of these business has opportunities to be meaningfully better. And part of that is this mix between corporate and business. The other part of is each business has a good opportunity that they're you know, tweaks - there will be tweaks within the businesses but each of the businesses have really good right to play opportunities and I think we need to get the business back to consistent, positive footing and expansion in each of these areas that we play in. I think down the road I think they're, you know, the kind of corporate strategy of how all these fit together I think is one that we can articulate in more detail in the past. I'm not going to, I think the strategy we've had, I'm sorry, detail in future, I think this strategy we had in the past is fine for now. Our focus right now is just execution and getting the businesses back to where they should be at a business level, and then I think we can have a long-term discussion about how they fit together.

Collin Verron: Any other more questions in the room? I guess my last one then on capital allocation, this is a little bit more near-term, but I guess how quickly can you get sort of, you talked about the near-terms target being below two and a half times, how quickly can get there, and then once you reach that level, how should we think about your view on capital allocations going forward? Is any different than past, than in historical Fortune Brands. So any kind of-

Jesse Singh: Do you want to take the timing?

Ashley George: Yeah, I mean, from a capital allocation framework, maybe just to step back for a second, we will focus first on incremental free cash flow generation. We'll make the organic investments in the business that we've been talking about, whether it's execution, product development brand, therefore there'll be less focus of M&A investment in the near-term. I'd say the balance will be share repurchases, balanced with getting to that net leverage target. So the 2.5 is the near-term target we've talked about. We should be approaching that and achieving that by the end of '26, and then we'll continue to evaluate where we go from two and a half, right? Over long-term, it's probably something lower than that. But I think from a near-terms perspective, we should be there by year-end.

Jesse Singh: And then to your, you know, what's different on the capital allocation. So, if you go backwards, we invested a fair amount on acquisitions. I think for at least the near-term, as I've highlighted multiple times, we like the three pillars plus the two adjacencies that we're in. If there were specific bolt-ons that would make those businesses better, we might consider it, but I think in general, our focus is going to be deploying capital against growth opportunities, I, you know, and I'm not guiding specifically, but obviously, software is, and the impact of technology is an asset, so maybe there's a little bit more capital there. Not meaningful, but incrementally more there. We don't spend a lot. We're not a capital-intensive business. We don't plan on becoming one. We've got plenty of assets. But if there's growth opportunities where we can organically invest, terrific, we'll do that. And then tuck-in acquisitions and then the rest is, you know, it would be appropriate to return that back to the shareholders in an accretive way. But obviously, if there's organic, you can get a great investment on organic and very selectively inorganic prior to that. And I'm not used to having a dividend, but it's part of our allocation to shareholders. But we need to also make sure that we do things like buybacks to be additive to that.

Dave Barry: I think the one thing I'd build, just to remind people, that it's not a very capital-intensive business, right? So we're in a normal state, three-ish percent of net sales for CapEx, about a percent of maintenance to balance for growth, cost out, product development, and then some capacity, but as we look across our network, we're pretty well-capacitized to capitalize on any volume upside that comes.

Collin Verron: Helpful. So I guess last call on questions in the room before we wrap up. All right, I really appreciate the Fortune Brands team being here, Jesse, Dave, Ashley, this was great and super helpful. Thank you.

Jess Singh: Yeah, thanks, Colin. Really appreciate it. Thanks for the time.