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RPM.N - Q1 2023 RPM International Inc Earnings Call

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PRESENTATION

Operator

(technical difficulty) 2023 first quarter. My name is Vaseem, and I will be your operator for today's call. (Operator Instructions) At this time, I would like to turn the call over to Matt Schlarb, senior director, investor relations at RPM. Please go ahead, sir.

Matt Schlarb

Thank you, Vaseem, and welcome to RPM International's conference call for the fiscal 2023 first quarter. Today's call is being recorded.

Joining today's call are Frank Sullivan, RPM's chairman and CEO; and Rusty Gordon, vice president and chief financial officer; and Michael Laroche, vice president, controller and chief accounting officer. This call is being webcast and can be accessed live or replayed on the RPM website at www.rpminc.com.

Comments made on this call may include forward-looking statements based on current expectations that involve risks and uncertainties, which could cause actual results to be materially different. For more information on these risks and uncertainties, please visit RPM's reports filed with the SEC.

During this conference call, references may be made to non-GAAP financial measures. To assist you in understanding these non-GAAP terms, RPM has posted reconciliations to the most directly comparable GAAP financial measures on the RPM website. Also, please note that our comments will be on an as-adjusted basis and all comparisons are to the first quarter of fiscal 2022, unless otherwise indicated. We have provided a supplemental

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slide presentation to support our comments on this call. It can be accessed in the Presentations and Webcasts section of the RPM website at www.rpminc.com.

At this time, I would like to turn the call over to Frank.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Thanks, Matt. Good morning. I'll share a broad commentary on our consolidated performance for the quarter, and then Mike Laroche will provide details on our financial results, after which Rusty Gordon will conclude our prepared remarks with our outlook. After our prepared remarks, we'll be pleased to take your questions.

Before I begin discussing our results, I'd first like to send our best wishes and thoughts to all those impacted by Hurricane Ian, including many of our own associates. We're all grateful for the first responders and safety professionals who are playing a critical role in keeping people safe and rescuing those in danger. As people in the affected area work to rebuild their homes and property, our Legend Brands disaster restoration business and our Tremco waterproofing business are responding to help return their lives to some sense of normalcy.

For example, in our Tremco Weatherproofing Technologies Inc. business, associates drove eight hours to obtain additional supplies in preparation for the storm and used, in one instance, chainsaws to clear downed trees to reach a commercial customer in need. These include hospitals and schools. Additionally, one of our supervisors in Central Florida, Steve Reeves, came in late Friday evening, the night before his son's wedding, to ensure that our crews would be able to patch a customer's roof Saturday morning. These examples demonstrate the commitment we take in serving our customers, and we will do our part to help the affected regions recover as quickly as possible.

Now turning to our results. If you look at slide three in our PowerPoint presentation, the first quarter was a positive one for RPM despite several market and macroeconomic challenges. Revenues grew by double digits in all of our segments to reach a record for the first quarter, and our adjusted EBIT margins recovered, resulting in all-time record high adjusted EBIT for RPM. While supply conditions remain tight, material availability did improve throughout the quarter. This is primarily a result of measures our teams have taken, including using our Corsicana, Texas plant for self-sourced raw materials.

Our R&D and procurement personnel have fought throughout the supply chain challenges by identifying new sources of raw materials and qualifying them to ensure our customers receive the quality products they expect from us. This collaboration, which is occurring across RPM's businesses, has allowed us to better meet customer demand, add resiliency to our supply chain and realize additional savings from our MAP 2025, Margin Achievement Plan.

During the first quarter, we generated $30 million of incremental MAP savings, which were a key driver in achieving record adjusted EBIT. The positive momentum in sales growth we achieved in fiscal year '22 continued during the first quarter of fiscal 2023. And I'm exceedingly proud of our associates' ability to overcome macroeconomic headwinds and supply chain challenges and convert this sales growth into expanded margins and improving profitability.

Turning to slide four, you'll see all four segments generated double-digit sales growth, resulting in record first-quarter revenue. Consolidated unit volume increased approximately 5%, while pricing on a consolidated basis increased on average of 15% as we work to catch up with continuing cost inflation that increased year-over-year 28% in the first quarter. Driven by operational efficiencies, including the $30 million of MAP 2025 savings, pricing initiatives in three of our four segments achieved strong adjusted EBIT growth, with our Performance Coatings Group and Specialty Products Group achieving record results, and consolidated EBIT margins expanded by approximately 170 basis points.

Looking at sales by geography on slide five, growth was led by North America, our largest market, which generated 80% of our first-quarter revenue. Demand in North America was strong, and we generated good sales growth across all of our segments. Emerging markets also performed well during the first quarter with double-digit revenue growth in Latin America, Asia-Pacific, and Africa, and the Middle East. Europe, which comprised 13% of overall sales in the first quarter, was the outlier with revenue down 8.5%, which drove operating earnings down in the region 35% quarter-over-quarter. These declines resulted from the challenging macroeconomic conditions in Europe exacerbated by rapid inflation. Our

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Construction Products Group and Performance Coatings Group, which have relatively sizable presence in Europe, felt the impact of these challenging market conditions most acutely.

I'll now turn the call over to Mike Laroche to discuss our consolidated and segment financial results in more detail.

Michael J. Laroche - *RPM International Inc. - VP, Controller & CAO*

Thanks, Frank. We generated record first-quarter consolidated net sales of $1.93 billion, an increase of 17.1% compared to the $1.65 billion reported in the prior fiscal year period. Organic sales growth was 19.5%, or $321.9 million. Acquisitions contributed 1% to sales or $16 million, while foreign exchange was a headwind that decreased sales by 3.4%, or $56 million.

Adjusted diluted earnings per share were a record $1.47 and represent an increase of 36.1% compared to the $1.08 reported in the year-ago quarter. Our consolidated adjusted EBIT increased 33.1% to an all-time record $275.3 million compared to $206.8 million reported in the prior-year period.

Our Construction Products Group generated first-quarter record net sales of $729.7 million, an increase of 13.2% compared to the fiscal 2022 first quarter. Organic sales growth was 15.8%, with acquisitions contributing 1.9% and foreign currency translation headwinds reducing sales by 4.5%.

Roofing systems generated strong growth and benefited from increased public sector spending, its turnkey service model and a focus on renovations. Admixtures and repair products for concrete also grew strongly during the quarter as the business gained share.

Geographically, Asia-Pacific markets performed well, while sales and earnings declined significantly in Europe and Canada, where CPG is more concentrated compared to RPM overall. Europe experienced severe inflation and macroeconomic challenges, while Canada was negatively impacted by strikes and concrete shortages that impeded the completion of construction projects and led to inefficiencies. These market challenges in Europe and Canada were key drivers of adjusted EBIT decline, which was down 5.1% to $111.2 million compared to $117.2 million in the prior-year period.

Additionally, the Corsicana plant rolls up through CPG and resulted in a negative financial impact during the first quarter as the facility increases production toward full capacity. FX and mix also negatively impacted EBIT. Partially offsetting these headwinds was pricing in response to continued cost inflation, which was a positive contributor to adjusted EBIT.

Performance Coatings Group's fiscal 2023 first-quarter net sales were a record $340.4 million, an increase of 19.2% over the prior-year period. Organic sales increased 23.6%, acquisitions did not impact sales, and foreign currency translation was a 4.4% headwind.

Flooring systems, protective coatings and FRP grating, all generated double-digit growth. These businesses are well positioned to benefit from the trend of reshoring manufacturing to the U.S. Additionally, energy markets continue to generate strong growth, as did emerging markets. Pricing management also contributed to the strong growth.

Adjusted EBIT increased 27.6% to a record $47.9 million in the first quarter of fiscal 2023. The growth was driven by positive volumes, selling price increases and sales management, which generated favorable mix. Partially offsetting these positive factors was foreign exchange, which was a headwind to adjusted EBIT.

Specialty Products Group reported record net sales of $202.7 million for the first quarter of fiscal 2023, an increase of 11.3% compared to the period a year ago. Organic sales increased 12.8%, acquisitions added 0.6%, and foreign currency translation was a headwind of 2.1%.

Record first-quarter sales were driven by strength in the food coatings and additives business, whose new management team positioned this operating unit to benefit from increased institutional demand as pandemic restrictions were lifted. The disaster restoration equipment business also grew its top line as we work through backlogs caused by previous semiconductor chip shortages. Selling price increases in response to continued cost inflation also contributed to revenue growth.

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SPG's adjusted EBIT of $29.6 million was a first-quarter record and an increase of 18.9% compared to adjusted EBIT of $24.9 million in the prior-year period. The increase was driven by improved sales and pricing, as well as fixed cost leverage resulting from higher production volume in the disaster restoration equipment business.

The Consumer Group achieved record first-quarter net sales of $659.5 million in fiscal 2023, an increase of 22.5% compared to the first quarter of fiscal 2022. Organic sales increased 24.1%, acquisitions added 0.4%, and foreign currency translation was a headwind of 2%. The Consumer Group's revenue growth was driven by improved supply of key alkyd resins produced by the Corsicana manufacturing facility we acquired last September, as well as from new suppliers who our teams worked hard to qualify. This increase in supply allowed us to better meet customer demand. Price increases in response to continued inflation also contributed to the strong revenue growth.

Consumer Group's adjusted EBIT in the fiscal 2023 first quarter was $117.1 million, an increase of nearly 150% compared to adjusted EBIT of $46.9 million reported for the prior-year period when sales and profitability suffered from severe supply shortages resulting from a plant explosion at an alkyd resins supplier. The growth was driven by MAP operational efficiencies that were realized as a result of the improved material supply.

Pricing increases in response to continued cost inflation also contributed to adjusted EBIT margins approaching long-term averages.

Now I'd like to provide an update on capital allocation structure. During the first quarter of fiscal 2023, we repurchased $25 million of shares and paid dividends of $51.4 million. These actions demonstrate our long-held commitment to enhance shareholder value by returning capital.

Turning to our capital structure. We took actions to enhance our balance sheet strength and flexibility. First, we increased the size of our revolving credit facility by $50 million to $1.35 billion and extended its term to August 1, 2027. This credit facility provides us the flexibility to implement strategic initiatives, including MAP 2025 and M&A. Additionally, we prepaid $50 million of our term loan and extended its maturity to August 2025 from February 2023. The outstanding principal on this term loan is now $250 million. As a result, we only have modest repayment requirements through 2026.

With that, I'll turn the call over to Rusty to discuss our outlook.

Russell L. Gordon - *RPM International Inc. - VP & CFO*

Thank you, Mike. As we look forward to the second quarter of fiscal 2023, several of the challenges we faced in the first quarter are expected to continue and possibly intensify. Supply chains are improving, both from our initiatives and market conditions, but remain tight, and any disruptions can delay the realization of benefits from the execution of our growth initiatives.

A strong U.S. dollar is expected to continue to be a headwind to both sales and adjusted EBIT growth, particularly in our CPG and PCG businesses, which have a larger percentage of their sales outside the U.S. From a macroeconomic perspective, Europe is expected to be challenged by high inflation and impacts from the war in the Ukraine. In the U.S., persistently high inflation and rising interest rates have increased the economic uncertainty and the possibility of an economic downturn.

Even with this uncertainty, we are confident that the strategic actions we have taken position us to succeed in the second quarter and beyond. These include: #1, actions to further improve material supply; #2, implementing MAP 2025 initiatives; #3, positioning our businesses to benefit from the reshoring of manufacturing to the U.S. and continued infrastructure and stimulus spending; and #4, diversifying our portfolio of businesses, which have limited exposure to China and autos, while focusing on sustainability, including maintenance, restoration and energy efficiency. As a result, we anticipate that second-quarter sales growth on a consolidated basis will increase 9% to 12%, led by Consumer, which is expected to continue to benefit from better material supply and pricing increases in response to continued inflation.

Fiscal 2023 second-quarter consolidated adjusted EBIT is expected to increase by 30% to 40% as we benefit from MAP 2025 savings and favorable comparisons to the second quarter of fiscal 2022 when we were challenged by severe supply chain disruptions.

This concludes our prepared comments. We will now be pleased to take your questions.

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Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Vaseem, can you please open the line for questions?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We will now take our first question from John McNulty with BMO Capital Markets.

John McNulty - *BMO Capital Markets Equity Research - MD & Senior U.S. Chemicals Analyst*

Congratulations, I mean across the board really solid results. So, I wanted to understand the Consumer business maybe a little bit better because it was definitely stronger than we thought, and I guess there were kind of two parts to that -- the top line and the margin side. On the top line, I guess how reflective is that of kind of the current demand environment? And is there like a catch-up? Because I know alkyd kind of held you back from stocking the shelves in the past. Like was there a little bit of a catch-up? Or are you actually seeing that kind of point-of-sale demand right now?

And then on the margin front, again, the margins definitely came back faster than we thought, and it seems like you've got an even better handle on the alkyd situation, or it came back faster than we thought. I guess, is that a fair characterization of the quarter? Were there some one-time things that maybe benefited you and maybe we shouldn't be thinking about this as a good kind of normal run rate going forward? I guess, how would you characterize that?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, John, let me start with some big picture comments that will then get specific to your questions on Consumer. So, I commented on our organic growth and the split, which is roughly 5% unit volume on a consolidated basis and 15% price. Neither we nor any of our competitors provide specific price detail at a segment level. But with that guidance, we had higher-than-average price increases in Consumer. That's consistent with the historic patterns of getting price typically at a six- to nine-month lag to what we get in other parts of RPM. So, you could see that in our results a year ago where we were really challenged and operating at historic low margin levels and low profitability. That was part of it. So, a lag in pricing relative to raw material cost increases, which we're now catching up on.

Second issue is clearly material. We moved aggressively to be able to source our own alkyd resins with the purchase of the Corsicana plant in Texas last September. And that has helped us significantly, we believe, to catch up on demand that we weren't in the industry, wasn't able to meet, because of this alkyd resins shortfall.

And then lastly, MAP 2025 is something that we have been working on for a year. And Rusty and I had hoped to introduce it and provide more detail before now. As you know, we have an investor day, which will be webcast on Friday, that will provide more details on MAP 2025. We were waiting for a more stable period of time. And it started to feel like waiting for Godot because there has not been a more stable period of time in the last two years, and I don't think it's very stable today.

I say all that because we have been designing and beginning to implement MAP 2025 over the last, let's call it, six months plus. And better than half of that work initially has been at our Consumer Group. And so, if you look at the adjustments of consulting fees and other fees, we had a lot to do with -- a lot of work to do on operating efficiencies and SIOP efficiencies, particularly in Consumer. So, there's been a lot of work on that in the last year. Those three things, I think, combined to generate the strong recovery at Consumer.

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The last comment I will make, and then I'll stop and answer additional questions, is that despite the strong quarter, only at our Performance Coatings Group are we operating at record EBIT margins. We are not back to record EBIT margins at Construction Products, at Specialty Products or at Consumer, so we still have some more work to do, both in terms of executing on MAP 2025 and on addressing cost/price mix issues that have been driven by the inflationary environment that we're in.

John McNulty - *BMO Capital Markets Equity Research - MD & Senior U.S. Chemicals Analyst*

Got it. No, that's hugely helpful on the color. Maybe I can ask just as the follow-up on the Construction segment, because you actually kind of pointed -- you gave a good segue on that. So, the margin in that one, when I look at 1Q was down about 300 basis points from the prior year and even the year before that. Now you highlighted a couple of different things that might have impacted it. So, I'd love to get a little bit better understanding on it. You mentioned there was a strike. There were concrete shortages. You also have the Corsicana plant that's now in here and maybe isn't kind of running on all cylinders quite yet. I guess, can you unpack how we should be thinking about the margin degradation in that business and how to think about that going forward as maybe some of these things reverse themselves?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, the Corsicana plant is owned and operated by our Construction Products Group. The primary beneficiary of owning that facility so far has been our Consumer Group, and in particular, Rust-Oleum relative to introducing acrylic resin production there. It carries a cost of about $3 million negative per quarter. And so, we're working to fill up that capacity, and we have every belief that we will do so successfully, both with some external production, as well as more internal production across some different chemical products. But right now, that cost is borne on the EBIT and P&L of our Construction Products Group.

Europe is something we talked about when we talk to investors in July, and our concerns have been borne out. Europe is in a recession. Our biggest exposure in Europe is in our Construction Products Group, whether it's in the U.K. and/or on the continent. And so, energy costs are a mess, inflation happened a little later and so a little bit bigger than what we're seeing now in North America. Our ability to get price there in the Construction Products Group, because of Europe, I talked about the average price on a consolidated basis of 15%, and the Construction Products Group was actually somewhat less than the average across all of RPM.

And then the Canadian situation surprised us, but I think it's circumstantial. This is a quarter that happened over the summer months. And as you'll recall, there were some significant trucking strikes. There also has not been new cement capacity in North America, particularly in Canada, for probably 20 years. And so there has been a cement and related concrete shortage that's particularly been a problem in Canada, although it is somewhat of an issue in the U.S. And that negatively impacted both the revenue base and the profit margin profile of Nudura in particular because concrete has been shorted to residential and light commercial versus infrastructure or more heavy industry.

Operator

Now we will move on to the next question. John Roberts from Credit Suisse, you can go ahead with your question.

John Roberts - *Crédit Suisse AG, Research Division - Research Analyst*

Congratulations on the quarter and look forward to Friday. Where are alkyd resin prices versus last quarter in a year ago now? Would you say alkyds are now in line with the other resins and will basically just follow oil prices with a lag?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

So I don't -- I'll let Rusty answer the specific there. I can tell you in the quarter, inflation was up year-over-year by 28% and sequentially from Q4 up about 2.5%. And I'll have to let Rusty for more specifics.

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Russell L. Gordon - *RPM International Inc. - VP & CFO*

Yes, alkyd resins, John, were more than double that, over 60% increase. What was the second part of your question, John?

John Roberts - *Crédit Suisse AG, Research Division - Research Analyst*

It's just where they are relative to other resins? And will they basically just lag oil prices from here forward?

Russell L. Gordon - *RPM International Inc. - VP & CFO*

Yes. And in terms of alkyd resins, those have been affected by a variety of raw materials besides oil. They do incorporate certain components of plant-based oils that we had difficulty getting out of Russia and the Ukraine. So, there's a number of things besides oil that will impact that.

As you probably remember, we had a major supplier outage over a year ago in North America. So, supply has been tight. We have ramped up in-sourcing at our Corsicana facility, but that does not take care of most of our requirements. It's a small percentage. So, we still rely on the alkyd resin market, and it's way up in inflation.

John Roberts - *Crédit Suisse AG, Research Division - Research Analyst*

And could you talk about your exposure to rising interest rates that offset part of the upside at EBIT?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. In general, I think Rusty and his team have done a pretty good job there. About 60% of our debt capital structure is fixed, with an average duration of almost 13 years and an average interest cost of 4.1%. And so, the latest piece of that was a 10-year bond that was done in January of this year at 2.95%. So, we've got some really solid interest rate protection there. The remaining 40% is floating rate and still at rates below our fixed rates. And part of our capital allocation strategy in the two-and-a-half-year period of MAP 2025 is to reduce some of those debt levels.

Operator

Our next question comes from Mike Harrison from Seaport Research Partners.

Michael Harrison - *Seaport Research Partners - MD & Senior Chemicals Analyst*

Congratulations on the nice quarter and impressive guidance. I was wondering if, Frank, you're willing to talk at all about the second half of fiscal '23 because you're doing something like 35% year-on-year EBIT growth for the first half based on your guidance and what you've just delivered. The comps do get a little bit more challenging in the second half, but I think we'd all appreciate maybe some initial thoughts on what EBIT growth could look like in the second half kind of based on what you know at this point, which I'm conscious that there's a lot of uncertainty out there.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, we provided guidance for Q2. And I think as we sit here today, we're pretty comfortable with that guidance, recognizing there's still tons of volatility. When we talk to investors in July about Q1, we did not anticipate the challenges that happened to our Construction Products Group in Canada, for instance. Again, we think those are circumstantial and behind us.

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So, the Q2 guidance is there. Given the seasonality of our Q3 and the benefits of our MAP 2025 program, I think that we're likely to have a pretty solid Q3 performance. Mike, beyond that, I think who knows. We are aware that fundamental primary chemicals have dropped meaningfully. That is not showing up in the paint coatings industries purchased chemicals yet. As I said, we've had 28% inflation year-over-year in Q1. What happens in Europe relative to the Russian war on Ukraine and its impact on energy costs and economic activity, particularly in the winter, is hard to know. So, I would -- it's impossible for us to venture beyond my comments.

Michael Harrison - *Seaport Research Partners - MD & Senior Chemicals Analyst*

All right. That's fair enough. And then I was wondering if you could comment on your fill rates within the Consumer business and maybe any shelf space wins and losses as you're kind of exiting this heavier season and starting to look at the next season.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. Depending on the product line across all of our Consumer Group, and this is principally a North American commentary, our fill rates range anywhere from the mid-70s to mid-90s. That is not at the 98% or 99% that our customers expect or that we delivered for decades, but it's substantially better than the 50% to 60% fill rates that we and others in our industry were operating at in fiscal '22 and part of fiscal '21 as a result of all the supply chain shortages.

So, there's been significant recovery there, and you can see that in our Consumer Group results. But we still have more work to do, and we are utilizing outside consultants on manufacturing and operations side in various places of RPM, but in particular, in our Consumer businesses to address some inefficiencies that popped up both in the midst of the Covid boom and then the challenges that everybody faced with the supply chain issues.

And just as a reminder, it was just in the third quarter of this last fiscal year and January of this calendar year, so December, January, that we had massive Omicron disruptions in our Pleasant Prairie plant in our Kenosha distribution center. Those are our two largest facilities across all of RPM, the largest facilities in Consumer. So, it's been pretty crazy. So, fill rates were up dramatically better, but not where they need to be yet, and we're working on that.

Operator

We have Vincent Andrews from Morgan Stanley for our next question.

Vincent Andrews - *Morgan Stanley, Research Division - MD*

Congratulations on the results. I have a quick follow-up on that last question. Just as I know it's category-capped, you have good access to what's going on in terms of retail takeaway. So, understanding what you said about the fill rates. But are you making any progress in terms of those store shelves, or is the product still going out the door faster than you can get it on the shelf?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

I think we're making good progress on store shelves. And I think you're, again, across the industry, you're seeing in comparison to prior-year periods declines in the low- to single -- mid-single digits in terms of consumer takeaway. So, there is some weakness in some categories at DIY. The flip side is on the Pro area. So that is more in our primers and in our DAP caulks and sealants. You're actually seeing the opposite, some low- to mid-single-digit unit volume growth because the Pro seems to be holding up pretty well.

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But DIY takeaway is somewhat less than last year - in recent periods is very volatile. And you can see one week to the next, where -- not fill rates, but consumer takeaway is up, and then a week later, it's down. So, there's a lot of volatility there in the DIY space, but some pretty solid unit volume growth in the Pro contractor space.

Vincent Andrews - *Morgan Stanley, Research Division - MD*

And just as a follow-up, you talked about the new management team. What in particular are they doing in the food coatings or additive space to sort of shake things up for you guys?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. Our Mantrose-Haeuser Group, which is part of the Specialty Products Group, is originally the business that created NatureSeal, which was a patented product that eliminated browning in sliced apples. And so, it really revolutionized the apple market, and we rode a great profitability on that for a long time until it went off patent. So that was a challenge.

We also acquired Holton Foods, a couple of other businesses that I don't recall off the top of my head, two or three other businesses that were relatively small, a business called PFI. And so, they were high-margin food coating and/or specialty sustainable food additive businesses. And we had the leader retire of the Mantrose-Haeuser business three years ago. The head of PFI, who actually was an owner who we bought the business from, ran that business for a couple of years. We have worked together with him to hire a really talented industry expert, who is pulling those businesses together on a more integrated basis in terms of our approach to the market, and it's working. And they're doing a really nice job there.

There's some exciting product areas. There's a product called VerdeCoat. It's in testing. It is a coating for cardboard that would eliminate the need for plastic clamshells. So, they have a lot of exciting things going on in that business. We've got a really talented industry expert that is now leading it and pulling together what formerly were good, but really independently operating businesses that were relatively small.

Operator

We have Steve Byrne from Bank of America.

Stephen Byrne - *BofA Securities, Research Division - MD in Americas Equity Research & Research Analyst*

You mentioned some consulting fees and so forth. So, what was the net earnings benefit of that? And perhaps more importantly, is that a sustainable earnings contribution in subsequent quarters? Or is this more of a one-timer? And I'm sure you'll get into more detail on Friday, but can you highlight anything in particular that you implemented to achieve that $30 million in cost savings?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

We will get into it in more detail on Friday. And we've got some good slides that provide that detail. And so, I don't want to get too much in front of that, and that will be webcast all that. Information will be available to both those people present, as well as people that are online. If you are present, you'll also get a tour of our Tremco Sealant business and get to see their test (inaudible). So we would encourage people to be here for that. I think you'll get some really good insights into some unique things that we're doing in our Construction Products Group.

Specific to your question, we have been working with outside consultants around big data management, particularly as it relates to cost/price mix. We have been working with folks in the Consumer Group on better efficiencies in our manufacturing facilities, and we are making good progress. That's particularly true at Rust-Oleum where we have more purpose-driven facilities around, for instance, large volume runs versus more specialty niche smaller runs.

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So, there's a lot of areas that we are really focused on. And they all are areas that should be gifts that continue to keep on giving, not onetime items. The original MAP to Growth program, a key element of that was MS-168, which is our manufacturing systems 168, and introducing lean manufacturing disciplines. Those efforts did not end with the formal end of the 2020 MAP to Growth program, which was May 31 of '21. They are continuing, and that is giving us incremental benefits at the plant efficiency line as well.

And I guess the last comment I would make is we have been developing and beginning to execute MAP 2025 over the last year. We just kept waiting for the world to get more stable before we introduced and committed to some three-year goals. And I guess, we decided that we'd be waiting forever. So, we will and very excitedly introduce more detail on the MAP 2025 program on Friday.

Stephen Byrne - *BofA Securities, Research Division - MD in Americas Equity Research & Research Analyst*

And Frank, any comment on what the EBIT contribution was from that? It sounds like whatever the cost associated with it has already been spent. So perhaps the margin benefit could expand from here?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

So it was $30 million in Q1. And again, some of that is a result of the MAP 2025 initiatives. And some of that is a continuation of the original MAP program initiatives. And I think we'll provide more detail and more guidance on what we expect in the coming years and, in some cases, for this year by quarter on Friday.

Stephen Byrne - *BofA Securities, Research Division - MD in Americas Equity Research & Research Analyst*

And Frank, if I can squeeze one more in here. You mentioned Corsicana is owned by Tremco. It sounds like fixed costs associated with that plant are not necessarily allocated to the other segments based on production. Is that right? And does that not reduce the incentives for cross-segment collaboration?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

No, we have a formulaic cost-plus approach to intercompany manufacturing and coordination, and that's what's being applied here. But one of the great benefits of our MAP to Growth program was the reorganization into four segments and four groups, and being center-led in manufacturing in this lean manufacturing disciplined approach, being center-led really to the point of centralized in procurement. And the data that was required, the data lake or data base that was required to allow that to happen.

And so, the collaboration and cooperation across RPM is a hell of a lot better today than it ever was. And so, your question, I think, sharply reflects following RPM for a long time and the fact that 10 years ago, that might have been a problem. It's not a problem today.

Operator

We have Arun Viswanathan from RBC Capital Markets.

Arun Viswanathan - *RBC Capital Markets, Research Division - Senior Equity Analyst*

I'm sorry, I was asking a question. I was wondering -- can you guys hear me now?

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Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes. Yes, we can. We're having some technical difficulties...

Arun Viswanathan - *RBC Capital Markets, Research Division - Senior Equity Analyst*

Sorry about that. So real quick, I was just wondering if you could help us understand, again, Consumer was well above our estimates. So, looking at that segment, if you could maybe split the upside that you saw between maybe alkyd resins availability improvement, price/cost and demand? How would you kind of characterize how the segment performed and your outlook, I guess, in those three buckets?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. Pretty much the comments we've made earlier. A disproportionate share of our early MAP 2025 initiatives have been focused on Consumer, particularly in manufacturing efficiencies. And so, we have picked up some manufacturing conversion cost efficiencies there. You'll recall a year ago that we talked about our gross margins were down in fiscal '22 in certain quarters by as much as 1,000 basis points, pretty dramatic.

And we had talked about how hundreds of basis points of that was just poor throughput because of the material shortages, because of some of the labor issues we faced. So, a combination of access to alkyd resins, and we think we have developed with Corsicana maybe some better access to alkyd resins than some competitors, and a more normal throughput in our plants helped overhead cost absorption as well. And then certainly, cost price mix. We got higher price increases over the summer in Consumer than we got over the summer in our other businesses because we were late.

So again, if you go back last year on a quarter-by-quarter basis, you saw really solid performance as we were gaining price in our industrial segments. And it took us that typical six- to nine-month lag to be able to start to catch up on the cost/price mix in Consumer. And you saw that, obviously, in the first quarter. So those are the primary drivers of our Consumer business.

We did have positive unit growth, which in this environment is not true in all consumer categories. And some of that's the nature of our businesses relative to small project redecorating, patch and repair and maintenance. And I think some of it is catching up on some of the supply shortages and fill rate issues that we've been improving upon since last year.

Arun Viswanathan - *RBC Capital Markets, Research Division - Senior Equity Analyst*

Great. And if I could just ask a quick follow-up. So, you've guided to -- it looks like about 16% adjusted EBIT margin in fiscal '25. Looks like over the last, say, five years, you've been more in the 11% to 12% range on an annual basis. So, it's a nice kind of 400 to 500 basis point uplift. Of that improvement, would you say that the progress would be equally split between the segments? Or which segments do you see the greatest opportunity? And that move, would that be ratable over the period, or would it be kind of back half weighted? Or how do you think about that?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, I can answer that from a big picture perspective. And then obviously, we'll provide segment results when we release those and talk about them in January. From a big picture perspective, we made really good progress in our 2020 MAP to Growth program. And we were a little bit behind the curve in terms of our goals. And then we got walloped by Covid and the supply chain challenges and took a big step backwards that you saw in our results, particularly in Consumer.

As volumes coming through our businesses, and as we're catching up on cost/price mix across all of our businesses, you are seeing us regain some of the MAP 2020 margin improvement that we obtained and is real but was impacted by supply chain challenges. And as I indicated earlier, the MAP 2025 program has been in the works for a year and been in execution, particularly with a focus on Consumer starting in January. And so, we're getting the benefit of that, and that will continue throughout fiscal '23.

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We expect positive sales and EBIT results in each of our four segments in the second quarter, but the volatility is such that beyond that, I wouldn't say much about -- further about our expectations other than what we'll realize and then report in more detail in January.

Operator

Our next question comes from Josh Spector, UBS.

Joshua Spector - *UBS Investment Bank, Research Division - Equity Research Associate - Chemicals*

Can you guys hear me?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes.

Russell L. Gordon - *RPM International Inc. - VP & CFO*

Yes.

Joshua Spector - *UBS Investment Bank, Research Division - Equity Research Associate - Chemicals*

Okay. Great. So, I just wanted to follow up on Europe specifically within Construction and Performance. The drivers there are pretty different in terms of the customer buying patterns. And I tend to think about Performance at least a little bit more linked to kind of industrial capex maintenance spending. So, I don't know if you can comment if you've seen that part of your market pull back equally to what you've seen on the Construction side or if they've been more similar. And then kind of related to that, I mean, most companies are talking about September got a lot worse versus August in the prior couple of months. Are you seeing that as well? And can you dimensionalize that versus the 8.5% decline you reported this quarter?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, first of all, Europe was a challenge for all of our segments in the quarter. And we have a sizable presence there in Consumer, Performance Coatings and Construction Products. The biggest piece is Construction Products. Your observation is spot on. There are different dynamics. And so, the Construction Products Group underperformed our expectations for the reasons we mentioned. Europe was a big piece of that.

So, on a relative basis, our Performance Coatings Group, while we struggled in Europe there, it was not nearly to the extent as our Construction Products Group because of their end markets. Oil and gas, more industrial capital spending. And I will tell you, we expect in Q2, and it is within our guidance, continued negative performance in the top line, bottom line in the European marketplace.

And I don't know that it's going to be any different than what we experienced in Q1, but we are a little bit anxious about the winter months and what it's going to look like when we get into the winter and then into the spring relative to the trajectory of the economy and its impact in Europe.

Joshua Spector - *UBS Investment Bank, Research Division - Equity Research Associate - Chemicals*

Okay. Maybe I could just try one other way just on the volume side, I guess, within Europe. I guess, if you were down 8% to 9% for the quarter, was August down meaningfully more? So, I guess, were volumes down there mid-teens plus or was it more ratable for you?

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Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes. I don't know that we would want to get into talking about a month, particularly a month in our second quarter. But again, I don't -- I think in Q2, we would expect a similarly disappointing or deteriorated performance that we saw in Q1. And so, it's a combination of weak economic activity. A meaningful contribution of it was the strong dollar and foreign exchange.

So, you're probably looking at a down 8% or 10% in the top line and a down comparable to the, I think 30% -- operating earnings were down 30%. I don't have -- we don't run EBIT and don't disclose EBIT necessarily by geography, but we thought it was important to highlight Europe because it was a key factor across all of our businesses, particularly in the Construction Products Group in terms of the challenges that we're facing, and that's going to continue at the same level.

Operator

Our next question comes from Jeff Zekauskas from JPMorgan.

Jeffrey Zekauskas - *JPMorgan Chase & Co, Research Division - Senior Analyst*

I think you said in the course of the call that your raw materials are up 28%. But in the...

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

In Q1, our raw materials were up 28% year-over-year, and they were up about actually 2.6% from quarter-to-quarter from Q4 to Q1. They are increasing at a lower rate certainly than what we saw in Q4 and Q3, but they're still up year-over-year.

Jeffrey Zekauskas - *JPMorgan Chase & Co, Research Division - Senior Analyst*

Yes. So, I was puzzled by that because your cost of goods sold is up 14.5%. And even if you take your MAP to Growth savings of $30 million and you add that back, then cost of goods sold is up 18%. So how can raw materials be up 28% if cost of goods sold is only up 14%.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

I would have to do the math and get back to you. Our cost of goods sold incorporate -- that basically our chemical cost of goods sold and incorporates freight, it incorporates other issues. So, I don't have a specific answer to you other than we did the calculation on our sort of primary raw material chemicals, and they're up 28%.

Jeffrey Zekauskas - *JPMorgan Chase & Co, Research Division - Senior Analyst*

Okay. And then in the year-over-year quarter, your SG&A was up, I don't know, $57 million. How would you divide that among the different segments? Was the -- was there any SG&A growth in the Consumer business? Was that kind of flat? And did volumes grow year-over-year in Consumer?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

So volumes grew in each segment except for our Specialty Products Group year-over-year. And the SG&A was relatively equal across all of our businesses. We don't disclose that level of detail, but they were consistent with a year ago. I think the thing that's benefited us during the MAP to

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Growth program, and quite honestly, through Covid, is there was a level of Covid-driven reductions in SG&A around travel and entertainment and other things.

And through the benefits of MAP to Growth, and also understanding certain Covid-impacted expenses, what was essential and continuing. So, for instance, we are again doing major sales meetings across most of our major businesses. Those were expenses we did not incur for the two years of '20 and '21 during Covid that we are recurring those. But the level of T&E is at a lower level than it was pre-Covid.

And so, I guess those are the comments I would have, but there's really nothing extraordinary in SG&A. We are building some SG&A talent, if you will, in our Specialty Products Group. And we are also building some SG&A in our Carboline business in both cases to address either opportunities for growth, or specifically with Carboline, to be more deliberate about expanding their base of business outside of their traditional oil and gas markets, which is really where they exceed and part of what's driving our Performance Coatings Group today. So, we have a number of growth initiatives that's driving SG&A, but nothing out of the ordinary.

Jeffrey Zekauskas - *JPMorgan Chase & Co, Research Division - Senior Analyst*

And then lastly, interest rates are going up in the United States. Is that making a difference to your demand profile in Construction Products? Does it seem that your order level has changed at all? Or as far as you're concerned, interest rates really aren't making much of a difference at all in going up to your demand?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes, it's a great question. We have some exposure to housing market now with Nudura. And so maybe our housing market exposure is a couple of hundred million dollars, and we didn't have much of it before in total. So that's certainly somewhat interest rate sensitive. But we had solid organic growth in our Construction Products Group in the United States. And it's an interesting dynamic, Jeff, relative to the types of things that normally you would have looked at historically in recessionary periods that would be driving activity.

And quite honestly, the fact that cities, counties and states are sitting on hundreds of billions of dollars, that have to be purposed from various stimulus. And so, the institutional work that we're doing with schools or hospitals and the infrastructure work is still pretty solid. And if the dynamics around all the stimulus is true, that should remain true in the United States for another year and a half or two years. And you can't even see the benefits yet of the $1 trillion-plus infrastructure bill that was passed. So, there's just some funny dynamics in this economy that don't fit with the normal type of indicators that you would have looked at in the past.

Operator

Next question comes from Ghansham Panjabi from Baird.

Ghansham Panjabi - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Can you hear me?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes.

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Ghansham Panjabi - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

I guess just as related -- a follow-up to the last question. The Consumer in the U.S. and Europe, it's clearly absorbing a fair amount of inflation. Some categories that are even Consumer staples have started to show some signs of demand disruption as elasticity sort of unfolds. How do you see that dynamic playing out for your Consumer segment over the next couple of quarters? I realize raw material availability has improved, but what about the demand destruction component?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, in general, I think we're seeing demand disruption in Europe, and that's obvious from our results. And we expect that to continue, and we're concerned that it could get worse in the winter relative to energy issues in the Russian war in Ukraine.

In the U.S., in particular, as I commented earlier, consumer takeaway has been volatile. From one week to the next, it's up 3% or 5%. Another week, it might be down 5% or 10%. So, it's very volatile in terms of where consumer spending is. I think we're doing better than other kind of DIY categories because of the DIY small project paint, patch repair, maintenance aspect of our products and also the kind of catch-up on the poor fill rate situation that we experienced in the back half of fiscal '21 and a good part of fiscal '22. So that's improving.

We are seeing -- and this is broadly inventory adjustments at all the big accounts. And again, so there's a lot of dynamics going on here. Inventory adjustments, but fill rates improving, volatile consumer takeaway is making for a very interesting dynamic. And so, I think that's why we're very confident in the forecast that we provided for Q2 but are still in a -- the business of forecasting quarter-by-quarter because to go out further than that is really impossible.

Ghansham Panjabi - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Yes, we're struggling with that as well. For the second question, on your comment, I think you said that raw materials were up roughly 3% or just under 3% sequentially. How do you sort of see that evolving 2Q onwards? And I'm asking because it seems like there could be some decorrelation between Europe since dealing with the energy prices of significance versus the U.S. If that is true, can you confirm that? And then second, are you fully caught up on price costs in each of your operating segments at this point?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

So I'll answer the last part. The answer is no. We were fully caught up in a number of our industrial businesses. And then I think people were expecting, particularly with some of the underlying primary chemicals coming down, that we'd see a flattening out. And so, in our Construction Products Group, in a few instances, we're behind the curve because of continuing inflation in Q1. We're getting there in Consumer. And again, that's more related to the lag that the people are aware of that has been true for us forever.

And so that, I think, that's an issue. We did have $30 million of benefit from the MAP 2025 program in Q1, and we will provide more detail on our expectations when we talk in our investor day on Friday, including over the MAP 2025 program, some anticipation of improving in the commodity cycle, which should benefit our margins. That's anybody's guess, but the current underlying lower levels of propylene and polyethylene, and ethylene, and some of the primary chemicals, which are down but have not translated into lower prices of the type of specialty chemicals we buy yet, are things that we'll talk about on Friday. And I think things that we anticipate should benefit margin recovery over the MAP 2025 program.

But the world we're living in today is still inflationary. The situation in Q1 is maybe surprising to some of our businesses, but it's the world we live in.

Operator

Our next question comes from the line of Kevin McCarthy from Vertical Research Partners.

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Kevin McCarthy - *Vertical Research Partners, LLC - Partner*

Can you hear me okay?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes.

Kevin McCarthy - *Vertical Research Partners, LLC - Partner*

Excellent. I wanted to talk pricing a little bit, Frank. So, you referenced the raw material cost increase of 2.6% on a quarter-to-quarter basis. Even in that context, are you continuing to seek incremental pricing at this stage of the cycle? And if so, where are you most encouraged or least encouraged by prospects there?

And if I zoom out the lens, do you think that very impressive level of 15% that you realized in the first quarter can be sustained for a little while here or do you think the comps just get too tough, and therefore, the price contribution starts to come down?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, I think we'll have solid contributions from price in Q2. It will start -- the benefit of price across RPM will start to -- it will still be positive but start to deteriorate in Q3 and Q4 as we annualize price increase actions that our companies took in fiscal '22.

And then unless there are further price increases, which would be in response to further inflation, I think we round the annualizing of pretty much all of our price increases by the first quarter of next year. And so, you'll see the impact slowly diminish after Q2, but still be positive. And that assumes that things stay stable as to where they are now.

Kevin McCarthy - *Vertical Research Partners, LLC - Partner*

Okay. That's very helpful. And I wanted to ask about your Legend Brands business. I think you referenced Hurricane Ian and some of the heroic efforts that RPM folks have been engaged in, in recent days. Can you put that event in context versus history? If I look back to Winter Storm Uri or Hurricane Harvey, how do these disasters tend to flow through the financials for that business?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, first of all, fiscal '22 was a particularly challenging, in the back half of '21, time for Legend Brands. They're oddly -- because they're in the equipment business, and over time it developed very sophisticated equipment that could be controlled remotely, were impacted by the chip shortage. And so that was an issue. And there really wasn't much in the way of hurricane activity or challenges in calendar '21 or in our fiscal '22.

It's certainly possible that an event like Ian could drive $10 million plus of a spiky revenue climb with pretty decent margin business over a, call it, a quarter and half or two-quarter period. So, it tends -- the response here is certainly going to be greater than 0. It could be $10 million plus, and it happens over, I will call it, a three- or four-month period, but it's not a sustained increase.

We've grown that business nicely since we bought it. They are selling their products into different channels and looking at some new product introductions. Those are the kind of things that lead to a steady increase on a business that's roughly $140 million. And then you can see these $10 million or $15 million event-related spikes over time.

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Operator

Our next question comes from the line of Mike Sison from Wells Fargo.

Richard Garchitorena - *Wells Fargo Securities, LLC, Research Division - Associate Analyst*

This is Richard on for Mike. One question, just maybe if you can give us some color on the commercial construction market, both in how it's impacted on CPG and PCG segments? And then maybe just sort of give us an outlook. You mentioned reassuring benefits, which you should see. Maybe also just visibility on the lead time that you get on that as well.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, our Performance Coatings Group is more driven by heavy industry, so oil and gas, marine, wastewater, water treatment, things like that. And that business from a demand perspective is doing very well. That's globally, as well as in North America. And we see that continuing because of the stimulus dollars I referenced, and where they'll go and the infrastructure dollars that are coming, and the onshoring. We do a lot of fab plants around the globe with our Stonhard flooring business. We do a lot of intumescent fire coatings.

One of the interesting things is we had some interesting big projects in the last year, a Tesla plant expansion, some Intel expansions, that were difficult to supply because of raw material shortages. The raw material shortages that impacted that are behind us for now, hopefully permanently. So, we're pretty bullish on the Performance Coatings Group dynamics for the foreseeable future.

Construction Products is related to the things I talked about earlier. There are just conflicting demand signals. Europe is a problem for our Construction Products Group, and that will continue. North America has been really solid, both some cost/price mix recovery and good unit volume growth. But we saw these unexpected, we think circumstantial situations around concrete supply, for instance, in Canada. Just an interesting challenge.

Right now, we are generating positive unit volume growth and some additional price benefit on top of that. Although as you saw in the quarter, not enough to get us back to record EBIT margins. Those things, combined with the benefits of MAP 2025, we would expect will drive positive EBIT results year-over-year in all of our segments, including our Construction Products segment in Q2.

Operator

There are no further questions. I would like to turn the call back to RPM Chairman and Chief Executive Officer, Frank Sullivan.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Thank you, Vaseem, and thank you, everybody, for your participation in our call today. Tomorrow at 2:00 p.m. Eastern Time, we will be holding a virtual annual meeting of stockholders. You can participate through our website at www.rpminc.com, and we would welcome your participation and your questions, which we will have a Q&A session virtually. We hope to return to RPM's in-person annual meeting, which has always been an exciting event for us in the fall of 2023.

We also have an investor day presentation on Friday morning. That is also accessible via webcast at www.rpminc.com. And in that investor day, we will highlight our sustainability activity and efforts. We will talk about our Construction Products Group in general. And for those present, I think, have a very interesting tour of one of our Construction Products Group sealant facilities and also provide details of our MAP 2025 program. So, we would welcome all of your active participation.

Thank you very much for your participation in our first-quarter call today and for your continued interest in RPM. Have a great day.

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Operator

This concludes today's call. Thank you for your participation. You may disconnect.

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