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Whirlpool Corp. (WHR)

Q1 2020 Earnings Call

CORPORATE PARTICIPANTS

Roxanne Warner
Head-Investor Relations, Whirlpool Corp.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

OTHER PARTICIPANTS

Michael Rehaut
Analyst, JPMorgan Securities LLC

Mike Dahl
Analyst, RBC Capital Markets LLC

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Sam Darkatsh
Analyst, Raymond James & Associates, Inc.

Curtis Nagle
Analyst, BofA Securities, Inc.

David S. MacGregor
Analyst, Longbow Research LLC

Eric Bosshard
Analyst, Cleveland Research Co. LLC

Kenneth Zener
Analyst, KeyBanc Capital Markets, Inc.

Seldon Clarke
Analyst, Deutsche Bank Securities, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by. Welcome to the Whirlpool Corporation Q1 2020 Earnings Conference Call. At this time, all participants are in a listen-only mode. After the speaker's presentation, there will be a question-and-answer session. [Operator Instructions]

I would now like to hand the conference over to your speaker today, Ms. Roxanne Warner, Head of Investor Relations. Thank you. Please go ahead.

Roxanne Warner
Head-Investor Relations, Whirlpool Corp.

Thank you, and welcome to our first quarter 2020 conference call. Joining me today are Marc Bitzer, our Chairman and Chief Executive Officer; and Jim Peters, our Chief Financial Officer. Our remarks today track with a presentation available on the Investors section of our website at whirlpoolcorp.com.

Before we begin, I remind you that as we conduct this call, we will be making forward-looking statements to assist you in understanding Whirlpool Corporation's future expectations. Our actual results could differ materially from these statements due to many factors discussed in our latest 10-Q and other periodic reports.

We also want to remind you that today's presentation includes non-GAAP measures. We believe these measures are important indicators of our operations as they exclude items that may not be indicative of results from our ongoing business operations. We also think the adjusted measures will provide you a better baseline for analyzing trends in our ongoing business operations.

Listeners are directed to the supplemental information package posted on the Investor Relations section of our website for the reconciliation of non-GAAP items to the most directly comparable GAAP measures.

Also, as we highlight on slide 2, there is significant uncertainty about the duration and potential impact of the COVID-19 pandemic. Therefore, our discussion of the potential impact of COVID-19 on the company's business results reflects our best estimate based on what we know today.

At this time, all participants are in a listen-only mode. Following our prepared remarks, the call will be open for analyst questions. As a reminder, we ask that participants ask no more than two questions.

With that, I'll turn the call over to Marc.

Marc Robert Bitzer

Chairman & Chief Executive Officer, Whirlpool Corp.

Thanks, Roxanne, and good morning, everyone. Before we discuss our first quarter business results, I'd like to take a moment to acknowledge the unprecedented circumstances we all are currently experiencing and the efforts we have undertaken as an organization to support our people, consumers and communities.

The health and safety of our employees continues to be our top priority as we navigate through this crisis. I'd like to take a moment to thank them for the hard work and ongoing efforts during this challenging time. These efforts began in early January with the creation of a cross-functional and cross-regional task force to aid in developing and driving globally aligned communications and action plans. In February, we took decisive action to ensure the safety of our 77,000 employees around the world, including banning all domestic and international employee travel while also ensuring our corporate and manufacturing locations abide by all local, state and federal guidelines and safety measures.

Additionally, we implemented our work-from-home policy, resulting in 95% of office roles now being performed remotely. Also, we continue to safely operate our plants and manage through periodic slowdowns and shutdowns as they arise.

As it relates to business continuity, we took decisive actions in late January to ensure we were able to continue supplying our consumers with our essential products and services. These actions focused on ensuring ample supply of critical components and detailed review of inventory across key product categories.

We also have remote-enabled call centers that allow us to maintain reliable post-purchase service to our consumers. Now, more than ever, families across the globe are relying on our products and services to take care of their families. They are depending on our products to clean, cook, and to provide proper food and medicine storage in their homes while also providing a place in the kitchen for them to come together as family.

Finally, we took a number of actions to give back to local communities in which we operate, including providing funding to support COVID-19 research in local hospitals, donations of PPE and appliances to hospitals and organizations, as well as providing additional donations to local food banks, shelters, and small businesses.

Overall, thanks to the strong actions and efforts of our teams, we've been able to significantly limit the number of cases in our companies around the globe.

Turning to slide 5, I'm highly confident in our ability to manage through these uncertain times, and I strongly believe that we have right actions in place to protect our operating margins and the financial strength to protect our liquidity position throughout 2020.

Thanks to the hard work of our employees and our relentless focus on delivering on our commitments to consumers, we delivered strong Q1 results, demonstrating our resilience as an organization.

As the depth and the duration of this crisis remains unknown, we are taking strong actions to mitigate the anticipated impact of volume deleveraging and sustain our operating margins.

Further, we have positioned ourselves well with ample liquidity and the financial flexibility required to weather this current crisis. Lastly, we remain committed to investing in our future while also taking actions now to win during the eventual economic rebound.

Now, I'd like to turn it over to Jim to review our first quarter results.

James Peters

Executive Vice President & Chief Financial Officer, Whirlpool Corp.

Thanks, Marc, and good morning, everyone. On slide 7, we show our first quarter 2020 highlights. We delivered organic net sales in line with the prior year with an ongoing EBIT margin and EPS of 6.1% and $2.82, respectively, highlighting the resilience of our global operations given the growing impact of COVID-19 throughout the quarter.

Our North America, Latin America, and Europe, Middle East and Africa regions demonstrated their strength and agility, delivering solid year-over-year margin results despite operational disruptions related to COVID-19.

Lastly, we delivered free cash flow improvement of approximately $100 million due to strong working capital management particularly in accounts receivable and inventory.

Turning to slide 8, we show the drivers of our first quarter EBIT margin. Price/mix negatively impacted margins by 175 basis points due to one-time product transition expenses and unfavorable product mix shifts due to COVID-19-related consumer purchases. As we highlighted on our Q4 call, we launched new lines of dish and laundry products in Q1 2020, driving a one-time transition expense of approximately 75 basis points.

Furthermore, as consumer behaviors changed due to COVID-19 safety guidelines, we saw increased demand for microwaves, low-end refrigerators and freezers, resulting in negative price/mix. Although we expect product transition expenses to return to normal levels in the second quarter, we expect these changes in consumer purchases to be a headwind during the crisis. This unfavorable margin impact was fully offset by accelerated cost takeout actions and favorable raw materials, leading to a margin impact of 175 basis points.

Lastly, strong cost discipline related to marketing and technology investments partially offset the impact of currency. Overall, we are pleased to deliver margins in line with the prior year. This is indicative of our strong cost discipline across the globe and we are confident these actions will continue to sustain our 2020 margins.

Turning to slide 9, I'll review our first quarter regional results. In North America, we saw a stable industry for the quarter and delivered net sales in line with the prior year. Additionally, we delivered EBIT margins of nearly 12% as strong cost discipline partially offset negative price/mix related to increased product transition expenses and lower mix related to COVID-19 consumer purchases.

In our Europe, Middle East and Africa region, we experienced positive industry demand across key countries through mid-February. However, the growing impact of COVID-19 resulted in operational disruptions and demand declines towards the end of February and throughout March, particularly in Italy and France.

We are pleased to see continued momentum from our cost reduction and strategic initiatives, which delivered the fifth consecutive quarter of EBIT improvement, with margins expanding 40 basis points, despite significant COVID-19 demand and operational disruptions.

Although we expect to see intensified demand pressure in the second quarter, we remain confident that our underlying business continues to make strong progress in our return to profitability.

In Latin America, we saw solid industry demand across Brazil and Mexico, along with strong share gains in Brazil, driving organic net sales growth of over 20%. EBIT margins were approximately flat compared to the prior year as strong cost discipline offset currency devaluation in Brazil. Finally, as a reminder, our first quarter 2019 results include the impact of the Embraco compressor business in Latin America's results.

In our Asia region, revenue declined over 20% as China demand declined sharply in the quarter due to COVID-19-related disruptions. This was followed by a government-enforced shutdown in India which has now been extended into early May. In China, our manufacturing facilities have returned to normal operating levels and we have seen demand stabilize with some initial indications of a rebound as consumers slowly reenter the marketplace.

Overall, we are very pleased with our first quarter EBIT margin results of 6.1%, given the approximately 150-basis-point EBIT margin impact from COVID-19. These results clearly demonstrate the agility and resiliency of our global operations.

Turning to slide 11, Marc and I will discuss our current perspective on 2020. I will now turn it over to Marc to begin.

Marc Robert Bitzer

Chairman & Chief Executive Officer, Whirlpool Corp.

Thanks, Jim. The broader macroeconomic environment continuing to rapidly evolve, the full impact of COVID-19 on our business results remain highly uncertain and we're unable to provide a meaningful full-year guidance at this time. That said, we want to provide the answers to three fundamental questions, which I'll go into more detail on the following slides.

First, what's the shape of a recovery? In this section, I'll provide an overview of the current sell-through trends in key countries, and an update on our full year net sales expectations.

We anticipate a U-type recovery throughout 2020, resulting in a full year organic net sales decline of 10% to 15%.

Second, can we sustain our operating margins? Here, I will discuss the fundamental difference in our margin profile entering the COVID-19 crisis compared to the 2008 recession and also highlight the additional cost actions we will drive throughout 2020 to help sustain our operating margins.

Thirdly, what's our liquidity position? Finally, Jim will discuss our strong cash and liquidity position, which will allow us to cope with the economic uncertainty we continue to face across the globe.

Turning to slide 12, I'll highlight the preliminary data that supports our perspective of a U-shaped recovery throughout 2020. Please note that we do not intend to share this data going forward, but we felt, given the uncertainty of the current situation, that this data will provide valuable proof points as we all assess the impact of COVID-19.

As we monitor the development of COVID-19 cases and its related impact on appliance demand within China, Italy and the US, we've begun to see similar U-shaped demand patterns emerge. China, we see clear signs of a U-shape demand pattern, with recovery closely linked, although slightly lagging from the reduction of new COVID-19 cases.

Turning to slide 13, while Italy's trends are not as mature as China's, the demand patterns are well in line. Turning to slide 14, even though the US is obviously at an earlier stage of battling the COVID-19, early signs point to similar U-shape demand trend as seen in China and Italy. It is important to note, however, that the demand decline in the United States is clearly not as pronounced as in China and Italy, and we are currently experiencing sell-out declines of around 20% to 25%, which is less than half of what we've seen in other markets.

We see two reasons for this fundamental difference in demand patterns. One, the US has a very significant portion of replacement sales of more than 50% of the total industry; and two, the home improvement channel kept stores open during this crisis, allowing consumers to continue purchasing appliances.

Based on the consistent demand trends we are seeing across three of our key countries, each at different phases of crisis, we are expecting a full year 2020 organic net sales decline of 10% to 15%, with a majority of the decline occurring in the second quarter, followed by a slow recovery in the third quarter, and a slight growth in the fourth quarter.

Turning to slide 15, the EBIT margin chart highlights the clear difference in starting positions entering the COVID-19 crisis compared to the 2008 financial crisis. In the quarters preceding the 2008 financial crisis, we delivered EBIT margins of about 5%. Upon entering the 2008 financial crisis, we saw EBIT margins drop sharply to around 3.5% before bottoming out at a negative 1% in the fourth quarter of 2008. Contrast this with our current starting point in which we recently delivered 2019 ongoing EBIT margin of 7% or greater from second quarter on and over 6% margins in the first quarter of 2020, inclusive of a 150-basis-point impact of COVID-19.

We are starting from a fundamentally stronger place due to the decisive actions we took post-2008 recession. We took many difficult but necessary actions related to the fixed cost structure of our business, including restructuring actions, plant optimizations and the exit of certain non-profitable product segments, ensuring that we would be able to withstand the next crisis. Since that time, we've remained disciplined in our approach to fixed cost management. Fixed cost discipline has structurally improved our margin profile, allowing us to enter this crisis in a position of strength.

Turning to slide 16, I'll discuss the additional strong actions put in place to sustain our margins over the near term. First, as our teams monitored the spread of COVID-19 from Asia to Europe and then to US and beyond, our operational teams acted early and decisively to ensure we appropriately matched inventory levels and our supply base to demand.

Second, we aggressively target significant reductions in both structural and discretionary costs, including a reduction in discretionary marketing and promotion spend and strict head count control across all regions, as well as unpaid leave, furloughs, among other actions. In parallel, we implemented a controlled trial process and put rigorous guidelines in place to manage our expenses going forward.

Third, we continue to focus on ensuring we capitalize on the deflationary raw materials market. Finally, we've maintained our strict focus on working capital management, ensuring we have the proper risk mitigation plans in place, dual sourcing strategies enacted and are appropriately managing our inventory levels across the globe. With these additional actions in place, we are now targeting over $500 million in net cost and raw material savings in 2020, up over $300 million from our previous guidance.

Moving to slide 17, I now turn it over to Jim to highlight our overall financial position and ability to weather this current crisis.

James Peters

Executive Vice President & Chief Financial Officer, Whirlpool Corp.

Thanks, Marc. As a result of the strategic actions we took leading up to this crisis, we entered the crisis with a strong balance sheet. First, we have a very strong liquidity position as evidenced by our current cash position of $2.8 billion, with approximately $2 billion available in remaining committed credit facilities. This is inclusive of a recently executed $500 million short-term credit facility.

Second, anchored by our strong balance sheet, we maintain ample buffer to withstand increased debt or a reduction in earnings without tripping our covenants. Our debt to capitalization limit is 0.65 and we are currently at approximately 0.5. While our interest coverage ratio requires a minimum of 3 times and we are currently above 10 times.

Third, we have access to additional levers to unlock cash. We continue to evaluate additional liquidity options. And from an operational standpoint, we will continue to effectively manage our working capital.

Fourth, I'd like to highlight that we refinanced €500 million of long-term debt in February of this year and have no additional bond maturities until the second quarter of 2021.

Furthermore, I'd like to remind everyone that we pre-funded our US pension in 2018, which effectively suspended our need to make further payments until 2023 or beyond. It is through our strong financial position and our continued actions that we strive to maintain our investment grade credit rating.

Lastly, I'd like to touch on our capital allocation plans, which have temporarily changed in light of our current situation. Although we repurchased approximately $120 million in shares in the first quarter, we will be suspending additional share repurchases until our future liquidity needs become clear.

That said, we did declare our quarterly dividend and remain strongly committed to returning value to shareholders through these difficult economic times. Overall, we are confident that we have the liquidity needed to support our operations during this crisis and remain focused on our long-term commitment to our gross debt-to-EBITDA goal of 2 times.

Now on slide 18, I'll turn it back over to Marc to discuss why we're well-positioned to win in the economic recovery.

Marc Robert Bitzer

Chairman & Chief Executive Officer, Whirlpool Corp.

Thanks, Jim. I'd like to take a moment now to discuss how we are well-positioned to capitalize on the eventual economic rebound in the short term, while simultaneously well-positioned for future growth over the long term. Throughout this crisis, where necessary, we have slowed our operations, adjusting operating line layouts and speed to adapt to government orders, new safety guidelines and dramatic shifts in appliance demand. This will allow us to quickly respond to positive demand changes and rapidly ramp up to normal level of operations.

Additionally, we anticipate there will be pent-up demand in the short term as discretionary purchases have largely been delayed. As a clear leader in home appliances across the globe, we are extremely well-positioned to capture this demand upon its return. To further take advantage of a recovery, we are leveraging our best-in-class manufacturing supply chain operations, remaining agile in our approach to production and inventory management.

As we look longer term, we believe that we are uniquely structured to take advantage of post-crisis demand changes. One of the changes we expect to remain is the rediscovery of the home and the kitchen as a center of living.

Needless to say, this will be a positive catalyst for our entire industry and our unmatched brand portfolio and innovation pipeline clearly give us a head start in capitalizing on this trend.

Additionally, we are anticipating an acceleration in the adoption of online purchasing for large home appliances post crisis. As such, the investments we have and continue to make in e-commerce and in direct-to-consumer sales as part of our digital transformation journey are key levers of our long-term growth.

Lastly, we remain committed to our ESG priorities. As highlighted in our recently released sustainability report, we have a long-standing history of investing in the safety and well-being of our employees and the environmental efficiency of our products and operations and in (0:33:27) support of the communities we call home.

In closing, I'd like to summarize our key messages on slide 19. We remain committed to the health and safety of our employees around the globe and will continue to adapt our policies and procedures as the situation with COVID-19 continues to unfold.

Our Q1 results highlight the strength and the resilience of our business, and we will continue to take decisive cost actions to ensure the health and viability of our business for the long term with a continued focus on sustaining strong margin throughout the crisis.

Additionally, we have ample liquidity to weather any demand recovery scenario and remain fully committed to driving our business towards our leverage goal of 2x over the long term.

Further, we are well-prepared to swiftly ramp up operations and leverage our global leadership position to win in the eventual economic recovery. It is because of these actions and the strong experience of our management team that we're confident in our ability to weather this crisis and emerge in a position of strength. We remain firmly focused on executing our business priorities and are fully committed to driving strong shareholder returns.

Now, we will end our formal remarks and open it up for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Michael Rehaut with JPMorgan. Your line is open.

Michael Rehaut
Analyst, JPMorgan Securities LLC

Q

Thanks. Good morning, everyone, and hope everyone is safe and healthy out there across your organization. Thanks for all the comments.

First, I was hoping to get a sense of decrementals, and I apologize if I missed that in some of the opening comments. But particularly what I feel a lot of companies have done – and by the way, almost none of them have kind of laid out their thoughts for a full year sales impact, so very much appreciate that perspective. But one of the other areas that I think has been helpful is to try and get a sense of how to think about decrementals in the second quarter, which certainly, generally speaking are the most extreme given some of the abrupt shutdown and inefficiencies that occur and how those decrementals might improve throughout the year as the cost savings that you've outlined that kick in?

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Michael, good morning first of all. Hope you all also are all in good shape and healthy and safe. Let me maybe just take your question and split it up to two pieces. First of all, obviously, everything depends now on the revenue assumptions. And the overall demand pattern, where we all recognize there is a very significant amount of uncertainty. But I think our perspective and today with the information which we have is a U-shape recovery on demand development, which means we expect the majority of the negativity in demand to occur in Q2.

I do expect a slight drag still in Q3 and Q4 recovery. So that gives you a little bit of a sense of what we anticipate from a broad demand perspective. That being said, that also means we have the biggest deleveraging effect on operations in the second quarter and maybe some elements also in the third quarter.

As we – and I think we mentioned that in some previous earnings call. Of course, the leverage effect you have on production is extremely different by production type, factory, occupational level, et cetera. But I think as a rough, and I underline a very rough rule of thumb, you can obviously assume about 18% to 20% is our leverage factor, i.e., every $1 you lose is about $0.20 of deleveraging.

I think it's however very important to highlight that in the significant increase of our net cost takeout, we already factored in the negative effect which we will have from our deleveraging. So that is all factored in on the cost side. Of course, the margin side is a different one. So we anticipate that we can absorb it, which is not going to be easy, and on top of that, increase our net cost take-out.

Michael Rehaut
Analyst, JPMorgan Securities LLC

Q

Okay, I appreciate that, Marc. And I guess – so if I understand your comments correctly, and it kind of leads me into the second question in any case. So just to clarify that response, are you saying that $500 million would negate the decrementals or would negate a worse-than-expected impact on the decrementals in the 2Q period, where you're going to have that higher level of inefficiency due to the abrupt nature of what's going on in 2Q?

And then the heart of the question for my second question really is, if you could give us a sense of the breakdown of that $500 million of net cost take-outs across the different buckets that you manage, then if any of those might be temporary, that you could layer back in in a 2021 timeframe, commensurate with improvement in demand?

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.
A

Yeah, so Michael, first of all, to clarify, the $500 million is the full year, and we haven't given the specification about how much comes in Q2 and Q3. But as you can imagine, it takes a little to ramp it up. But to be clear, the $500 million is after already all these inefficiencies. So that is net-net of everything. So it's a pretty clean number. So it's after the negative impact of deleveraging.

In terms of a composition of the $500 million and as you may recall, in the opening earnings call of this year, we roughly indicated about $200 million. So what you have in between – first of all as you indicated, you lose some. And that's the inefficiencies, which are – I mean, you take the number which we gave you before. And you also have a negative currency impact because a lot of materials we buy, for example, in Brazil, we have a negative currency impact.

On the good side, you have a slightly better raw material, which we have factored in. But then in addition, we have very significant expense control, expense management, SG&A efforts and also people cost. And that is a combination of both, to your point, kind of temporary actions but also structural actions. So it's not only temporary actions. So there is quite a bit of structural cost take-out, which we have factored in this $500 million. But again, I want to re-emphasize, after all these negative deleveraging effects.

Operator: Your next question comes from the line of Mike Dahl with RBC Capital Markets. Your line is open.

Mike Dahl
Analyst, RBC Capital Markets LLC
Q

Good morning. Thanks for taking my questions, and also I hope you guys are all safe and well. Marc, just a follow-up on the last line of questions; I guess, if I'm thinking about that bridge and applying 20% decrementals on your full year sales guide, and then adding back some cost take-out, it seems to suggest that the math would get you to EBIT that's only modestly down for the year and I think margin percentage would actually be up.

So I guess I'm just struggling to bridge that a little, because a number of other companies have talked about more like 40% decrementals, 2x normal, and then after a cost takeout, maybe getting back towards normal. So it just seems – I appreciate you guys have the raw mat tailwinds, but it seems a little out of sync with what we're hearing from some others. So maybe a little more color on that, please?

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.
A

So it's – Michael, let me first start and maybe Jim is also going to add to this one. First of all, specifically on the question on raw materials, yes, we see a slightly more positive tailwind from raw materials. But as I mentioned before, keep in mind, about half of that additional tailwind is already eaten up with currency losses.

So on the full year base compared to what we had before, maybe gives you a 0.25 point to 0.5 point more takeout from pure raw materials. But it's not as dramatic as you may assume because steel prices are largely locked in because these are annual contracts. You have a little bit of incremental benefit on plastic and resins, but that's about it.

Having said all that, so yes, our $500 million net cost take-out, that is our big lever which we have to protect our operating margins. We have not given and will not give a full year margin guideline, because there's a lot of other parameters coming into place. But yeah, that's our tool to protect our margins. But keep also in mind you have even on the top line, not only the overall revenue growth, but the mix, which – and that is not very untypical from the prior recession, the mix you should expect throughout the crisis is slightly negative.

So you can't anticipate the same kind of positive price margin effect as we've seen in the last one or two years because an economic crisis is not necessarily the environment where you get a huge positive mix. So you have a negative mix also in the full year assumption.

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

A

Yeah. I mean – Mike, this is Jim. And just to kind of reemphasize what Marc said is, I mean, you can already see in Q1, we're seeing the benefits of some of the reduction in raw material costs. And as we said, we extrapolate that across the year. That's about where we expect to be.

The additional cost savings will continue to build throughout the year, but we're not giving any further guidance beyond that, just due to the macroeconomic factors that we really can't predict at this time. And there are things in there such as currency and other things that are very highly unpredictable right now.

Mike Dahl
Analyst, RBC Capital Markets LLC

Q

Okay, thanks. That's really helpful. And then second question, and again, these weekly charts depicting some of the trends are really helpful, especially showing the beginning of recovery in China and Italy. So thank you for that.

Marc, I think you said that sell-in, or sell-out was tracking down 20% to 25% in the US and in the chart, it seems like it was more mid to high teens. So, I wanted to ask if your comment on 20% to 25%; is that in dollar terms including negative mix and is the – versus the chart maybe in units? And then could you comment on what your sell-in looks like relative to the sell-out right now in North America or US specific, please?

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Yes, so Michael, I mean just on the sell-out charts, and as I mentioned in our prepared remarks, we usually wouldn't include these ones, but given that we're all trying to read into how will the demand shape up, what kind of recovery we see for us, sell-out is still the best early indicator of what we're likely to see happening and we have it at least for our products in Italy and US. We have it on a weekly basis and that's why we for once in a while want to share it with you, just to give you also same kind of information as we look at it every day.

With that in mind, in particular on the US question, the 20%, 25% is revenue-related because as you highlighted, on top of volume, you have a slight negative mix. And again, that's not atypical for these kind of recessions. I think it's – and I want to reemphasize what I also said earlier is I think what we – and that's good news, well, relatively speaking, good news relative to some of the other markets.

We do not see the US market dropping as much as we've seen in Italy, France, or China. Very simple because of the high degree or high percentage of replacement demand and the fact that we still have the home improvement, but also some independent retailers open right now. So, the consumer has a place to go and fulfill that replacement need. And that's a fundamental difference in the US compared to many of the other markets which we see throughout the world.

Operator: Your next question comes from the line of Susan Maklari with Goldman Sachs. Your line is open.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Thank you, Good morning, everyone.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Good morning.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

My first question is just thinking also not just about the decremental margin, but the incremental margin. And with all the benefits that you've done in terms of the cost structure, just the $500 million, but then also just thinking about the last several years, what you've done with the business, how should we think about the incremental margin as demand starts to come back and to normalize a bit? Should it be higher, better than it has been in the past, and especially maybe thinking about the 2008, 2009 scenario and when you came out of that.

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

A

Well, Susan, here is what I would start with. I would say that to begin with, as the volume begins to come back, the incremental volume that comes back, you should assume at the 18% to 20% that we kind of quoted earlier, and that's how it will build back.

Now, over time, we will see the benefits of the cost take-out running in and that will help our margins in the long run. And again, if you look back to 2008 and 2009 and what we did with fixed costs back then, and we're able to keep it out till now, it will be the same thing as we continue to reduce our cost level, but those will be benefits that will be seen more in 2021 and beyond as things begin to stabilize.

I think the other unknown as I talked about this year is we do have a lot of currency fluctuation within there that could also have an impact on our bottom line at least in the near term. So, I think just for the remainder of this year, you should start to think about incremental volume in the 18% to 20% type of range.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Okay. All right, that's helpful. And then can you talk a little bit to Europe? Obviously, there's a lot of moving parts there now. Just how do we think about the work that you've done on the cost side relative to, obviously, the current conditions and maybe how that can trend as Europe starts to reemerge and you start producing there again.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Yeah, Susan, just on Europe. So first of all, Q1, you need to keep in mind Europe was impacted earlier than, for example US, from the COVID crisis. And the depth of the demand drop has been more severe than we right now see in the US. I mean, again, we saw Italy the numbers, and they will be very similar, if you look at markets like France or some of the other markets.

So the impact has been earlier and even stronger. Now in a certain way, you can look at the Q1 numbers even though in absolute terms, we still made a loss. But it was better year-over-year. In a certain way, that tells you how much progress we've done in the cost take-out in and getting this business in a much better structural run rate. Because as you can imagine, with these kind of volume drops, under normal circumstances, you would have a very, very negative impact even year-over-year.

So I would see – in a way, I would even see Q1 as a confirmation, we were on the right track, the cost take-outs were on right track. We've got to get through a storm which will also be obviously very severe in Q2. But structurally, from a pure cost take-out and how we refocus on the business, I still believe we're on a really right track here.

Operator: Your next question comes from the line of Sam Darkatsh with Raymond James. Your line is open.

Sam Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

Good morning, Marc, good morning, Jim, and I wish you both good health as well as your entire organization obviously.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Thank you.

Sam Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

A couple questions, if I might. Didn't really talk about Latin America at all either in terms of April trends and/or what you're seeing in the Mexican geography both in terms of demand, as well as some of the forced production shutdowns that we've seen in other areas. Could you help add some color to that geography?

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

A

Sure, Sam. Maybe I'll start off with this. One, what we saw in Q1 within Latin America and we talked about, we actually saw organic sales growth within Q1. So Latin America was probably one of the least effective regions even heading into March. And so we're just beginning to see the downturn there as we've seen some of the retailers shut in Brazil and other places.

And I'd say what we're seeing, at least from an initial sign is that that curve isn't much different, it's just to what level that curve will go but it's not much different from other parts of the world in terms of the rate that it's going. And that's why we don't really show anything on Latin America right now because it is a little bit further behind.

The second thing is, obviously, within Mexico, we continue to monitor the situation and certain products have been deemed essential, and certain products haven't. But also, we continue to monitor our supply chain there as we don't see any significant issues yet due to that.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Yes, Sam, it's Marc. Let me maybe expand a little bit on the supply question and go beyond Mexico. In very simple terms, you've got to look at the supply chain stability from two perspectives. One, how do you keep your factories up and running? And two, how can you make sure your components keep on coming into the factories.

On the factories, we made early on the conscious decision to keep our factories running even though at a much lower pace and much lower volume. And in a certain way we basically ran them very inefficiently because we – our assumption is that even a slow but steady supply chain is better than a stop-and-go.

Now obviously, we still had to follow sometimes certain government lockdowns or in some cases, we had to clean and sanitize a factory, but at any given time over last weeks, we had 80% to 85% of our factories running. So the factories are in a pretty stable and good situation.

Now in components, as you can imagine, our first focus on components supply and steady was related to China. That was our first area of concern. And I would say with an extraordinary amount of effort and hard work our team was able to get the supply chain situation in China in control. And we did not – not without challenges, but we did not experience any significant component shortages coming out of China.

Right now, our focus, as you alluded to, is a bit of Mexico, because the Mexico guidelines have not been synchronized with the guidelines of Canada and US. So we had some issues of stop-and-go of certain suppliers. I think they're being worked through, but they have not been completely resolved, but we remain confident they will be resolved in the next coming weeks.

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

A

Yeah. I'd say, the other thing, too, Sam, as we look at just the mix of product that comes out of Mexico, especially into the US, refrigerators have been deemed essential there, and that's a big part of the mix that we bring up from Mexico. And so there's no disruption in that supply chain at this time.

Sam Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

My second question, if I might. I apologize for rehashing this from other questioners, but it's pretty important and material to numbers. I just want to make sure I understand. So you would have us take 20% decrementals and then add to that, call it, the extra $300 million of cost take-out? I just want to make sure that everybody's math is accurate, and if you could be specific? Thank you.

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

A

Yeah, Sam, I think you're thinking about that the right way, because we have said we'll increase $300 million more of cost take-out but you've got to take that volume piece out on top. And within – that's the volume that comes out of the margin side. As Marc alluded to earlier, said there are costs due to the lower production, but we've already incorporated those into our net cost and that we will fully offset many of those with other cost savings around the company.

Operator: Your next question comes from the line of Curtis Nagle with Bank of America. Your line is open.

Curtis Nagle
Analyst, BofA Securities, Inc.
Q

Good morning, everyone, and thanks for the question, and thanks for all the details provided. So I just wanted to go a little bit more into I guess, a recovery path, and what gives you confidence in what I think sounded like growth in 4Q, I understand the sequential nature of improvement here, and again, the charts you showed are really helpful.

But is it perhaps a bit premature to call that? I guess, the reason I say that, particularly in, I guess any region, but you certainly look at the United States, I think you're expecting pent-up demand, but given where unemployment probably still will be and consumer confidence, is it reasonable to assume that growth comes back in 4Q?

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.
A

Yeah. So Curtis, first of all, we were first ones to admit, we don't know, okay. I mean, if anybody knows exactly the shape of a recovery, then good luck. As you know, there has been all letters of the alphabet being used to describe a potential form of recovery. And what we're seeing is right now, we believe the most likely scenario is a U-shape recovery, but that's not a certainty.

What I – before I get to the U-shape, what I would exclude right now, I would say, very low probability, the V-shaped recovery. I know there are some folks talking about it. It would be – we would love to see it. I just don't think it's happening. And at this point, you also cannot exclude an L-shaped kind of development of this whole crisis. But again, I would argue the odds right now which we see are in favor of U-shape.

The reason why we say that is, again, as I mentioned before, for two reasons. One is the early demand patterns, which we see coming out of the China market, some European markets clearly point toward the U-shape. And it's very different from financial recession because the depth of the crisis is more severe than financial crisis, but it appears from what we see from these markets that the kind of duration of the crisis shorter.

The other reason, and again, that's probably more macroeconomic, we should also not lose sight of the – that coronavirus falls on a different environment than it did in 2008. There is no housing bubble. Quite the opposite. The financial institutions are in a much stronger shape than we were in 2008. I think it's a different macroeconomic context where the coronavirus happened. But again, that's right now our most likely assumption. I think time will tell, is it a U, is it an L? We believe it's a U, but not an immediate recovery before Q4.

Curtis Nagle
Analyst, BofA Securities, Inc.
Q

Okay, fair enough. And then just wanted to go into a little more detail on the mix pressure. So Jim, I think you'd mentioned you're seeing higher volumes of some lower margin product. But what about – I guess, kind of likes-for-likes, are you seeing trade down in some of the core large appliance products you guys sell?

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

A

Well, Curt, as I stated, some of – what we saw in the first quarter if you broke it down, was that we did have some new product introductions, and that's something that we do see going away. But those were things we've talked about in the past and having about a 0.75-point impact on our margins.

The mix down that we saw, the bulk of it was selling more freezers, microwaves and lower-end refrigerators which is typically a sign that we see as people are preparing to stock up on more goods within their home and carry those kind of things.

I'd say, as we look forward throughout the rest of the year, obviously, there still will be a little bit of a mix impact due to that type of what we call a crisis-type mix. Additionally, depending on the economic situations, what you'll see is a lot of – duress purchases will continue. And many of times, in some of the more difficult times, duress purchases do mix down a little bit. But overall, we don't think that will be a significant impact on the rest of the year.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

And Curt, just maybe just an addition, because I think you may have also alluded to the promotional environment, I would say, compared to other periods, it's not very intense. And that's just the nature of that demand, the duress and replacement customer, they're not attracted by "deals."

And so right now, it's not a very intense promotional environment from that perspective, but yes, there is a fundamental, slightly different product mix, which is being sold through crisis periods.

Operator: Your next question comes from the line of David MacGregor with Longbow Research. Your line is open.

David S. MacGregor
Analyst, Longbow Research LLC

Q

Hey, good morning everybody.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Hey, David.

David S. MacGregor
Analyst, Longbow Research LLC

Q

And just listening to the taped lead-in at the top of the call as we were all waiting to get on and listing out all the things that you're doing around the world to help out was pretty impressive. So, thanks for what you guys are doing there. I hope Elizabeth Warren's listening.

I wanted to just ask you about the $500 million and see if you could lay that out by segments and give us a sense of just does it map roughly in step with revenue proportions or how should we think about allocating that out?

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.
A

Yeah, David, I would say that's typically the safest way to do it because right now, we're attacking costs in all regions of the world. But if you just take raw material costs, it's typically pretty ratable across the globe on what the impacts are.

Obviously, if you look at things like currency, you would weight those more heavily, especially to the Latin America region, where they're seeing a very significant impact there. But I think that's probably the best way to think about it.

David S. MacGregor
Analyst, Longbow Research LLC
Q

Okay, and then I guess, just following up on a previous question with respect to European costs. I guess I wanted to ask more about the top line in Europe. And just where does this leave you in Europe as you work to rebuild your listings?

And as you come out of this whole thing, do you pick up with the trajectory you were on before the virus or does this provide you with an opportunity to leverage your scale advantage and kind of accelerate, I guess, the recovery of the market share?

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.
A

And David, of course, well, we now need to see how Q2 the demand patterns evolve in Europe. But it's even – one or two smaller comments. Even in this sell-out chart which we showed for Italy, and that is our sell-out. So you also even saw the beginning of the year, we actually picked up nicely volume until the virus hit. So we actually felt pretty confident, and that's just Italy, but I would say we have seen similar developments in other markets.

So we started the year pretty well which is probably a good indication of the listings which we got with different retailers. But now we, of course, like everybody else, have been hit with the virus. But I'm actually pretty confident that we can pick up on where we started in Q1.

I would also argue, because of a very, very strong supply chain management in Europe where we limited the number of factory closures really to the bare minimum, our supply base inventory situation and stability of the supply base is actually a pretty good one. So we're confident we can get out of the gate pretty good. We have good availability, always with some limitations, but given what the overall crisis did to everybody, we're in a pretty good shape to come out of this one.

Operator: Your next question comes from the line of Eric Bosshard with Cleveland Research. Your line is open.

Eric Bosshard
Analyst, Cleveland Research Co. LLC
Q

Good morning. Thank you. Two things curious about; first of all, in the US, could you help parse a bit what you're seeing between channels? I think you commented earlier about the home centers remaining open, and that's helped sustain sales in the US relative to other countries. But could you talk a little bit about by channel how things are performing in the US?

And then secondly, could you just frame or scale a bit what the mix outcomes could be in 2020? Obviously, mix, price/mix has been a positive margin contributor. Marc, your comment about the down 20% to 25% relative to the units and talking about mix in that, could you just give us a little bit of comfort of what ranges the price/mix could be in 2020 either on a revenue or a margin impact?

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Yeah, so Eric, so first of all, on the US channel, of course, that is heavily impacted simply by the fact which stores are open and which ones are not open. As you know, first of all, from a broader environment, the US market is, compared to other international markets, still with heavy buys on in-store as opposed to the e-commerce market, which, of course, right now, in the crisis, the e-commerce side has increased quite a bit, but it's still a very store-based shopping purchase in the US.

So as such, what we saw in the channels right now is heavily driven by which stores were open. And that's just reality. And a lot will depend on Q2 in terms of at what pace do closed stores come back online and are reopening. And that's I think how you should read it. But right now, in the broader scheme, yes, by definition, what we saw in March and April, there is a heavy shift towards the home improvement channel in the US. And again, that's entirely driven by store openings.

To your point about the mix, and again, it's not atypical what we saw there versus 2008 and 2009. Particularly at the outset of this crisis, you see a heavy mix down. And particularly now there was – when people were hoarding, they bought a freezer, they bought a second fridge, and these don't come with high mix.

Typically, and what we see also already happening in China, that starts stabilizing as the crisis progresses. But for the premium and super premium purchase to then pick up, I think you will still have to wait a couple quarters. And then again, that's not entirely surprising because that's a discretionary purchase, which is often really driven by an entire kitchen remodel. So I think until we see the really rich part of the mix coming back, I think we will talk a couple quarters.

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

A

Yeah. I think just to kind of add to what Marc said is the 0.75 point that we saw due to the new product introductions, we had anticipated that. And that was built into our estimate at the beginning of the year. But Q1 and Q2 is when we'll see more just the shift in mix due to the crisis. And then that will eventually come back to a more normal level.

Operator: Your next question comes from the line of Ken Zener with KeyBanc. Your line is open.

Kenneth Zener
Analyst, KeyBanc Capital Markets, Inc.

Q

Good morning, everybody.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Morning, Ken.

Kenneth Zener
Analyst, KeyBanc Capital Markets, Inc.

Q

Just want to follow-up for the US mix, so we're talking, the replacement cycle, you believe, is supporting less volatility. But could you talk about – and you talked about the negative mix in terms of lower price points and I guess [indiscernible] (0:52:28). So could you talk about the discretionary component, which could be consumer confidence [ph] is sweet (0:52:37), which are probably impacted by – I know you've made comments about that, that's probably like a large kitchen remodel.

And then could you talk about your view, given you're involved with new home construction delivery of appliances. If you could just kind of go into those to give us a sense of how the actual shelter-in-place and distancing has affected those lines, thank you.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Yeah. So Ken, first of all, on the replacements, as we said in earlier conference calls, right now for 2020, we assume that the replacement part of entire industry demand is more than 50%. I think it was 52% or 53%, what we gave you as a number.

So if we see a market decline, that comes out of the non-replacement side of a business, so as a percentage it's now even higher, but in absolute terms, that's a pretty steady number from replacement. And we also clearly positioned that replacement side almost as a floor of the market because we're still comping against the low years of 2008, 2009, 2010. So we feel pretty good. That's the floor, and it will not drop a whole lot further. So that's a steady side.

The high end discretionary one is, I think, where you in the short term, and I would say, two to four quarters, you will see still some negative, and that's not surprising, and by the way, very, very similar to what we had seen in 2009 and 2010. Particularly in your question about the new homes and the builder channel, keep in mind we are at the very tail end of any house completion. Appliances are one of the last products which come into any build.

And as you all have seen with the builders, the builders had a very strong order intake and starts pretty much until early March, mid-March. I think there has now been some drops in late March and April. But the projects and the houses which the builders have started, they will complete. So we do see from our side certainly in Q2 and Q3 still a very steady stream of new homes and what we do there with the appliances.

The key question, of course, is then how does the broader builder market now develop. And I think there's arguments made why it will continue to grow, like the low mortgage rates and fundamental demand still. But of course, consumer confidence will play a key factor. As long as this overall recession is limited in duration, I don't think we will see a major lasting impact on consumer confidence. But of course, that's one of the big uncertain elements right now.

Kenneth Zener
Analyst, KeyBanc Capital Markets, Inc.

Q

Thank you for that. Jim, I'm going to go back to – it's been asked a couple times, because it's rather astounding the implication for your margin degradation. But looking again at just North America, in 2008, your sales fell about 10%, you had about a 300-basis-point decline in margin, realizing margins were different in terms of the base level. But specifically, I mean, we keep going into this. So, your fixed costs are lower. You guys removed a lot of fixed costs last cycle. With the cost – so obviously, a lot of your 20% – you have a lot of variable costs.

So, with the material declines that you including the $500 million, can you just – is it really that fixed cost is different that is supporting the math because the labor – the material costs have fallen but is it really the fixed cost that is so different in 2020 as sales are down high single digits in the US versus what we saw in 2008? Thank you.

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.
A

Yeah. Ken, here's what I'd say is what we've talked about with the fixed cost is when we took those fixed costs out in the 2008 to let's say, 2011 time period and improved our margins as they began to grow back in 2012 and beyond is we kept a lot of those fixed costs out.

And so what you were seeing is that we kept the fixed cost as we grew revenues and grew volumes across the globe and especially within the US and now as we've had the decline, it's not as significant as it was back then as an impact to our bottom line because of that already low fixed cost base we're starting on.

Then in addition to that, as we talked about is we will target taking out and we will take out additional costs here. Now, some of those will be fixed, some will be variable and that's just how you've got to look at it go forward.

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.
A

And Ken, let me maybe add off an additional comment on this one is – and that's also why we included this chart where we compared 2008 and the current crisis.

First of all, if you compare 2008 to the current one, the starting point of our margins in 2008 coming into the crisis were lower. And as you've seen on my chart, in the first quarter, as a company in total, not North America, we basically barely made a profit. Actually, we had a small loss on the EBIT base.

Now fast-forward to the current one, the volume drop right now and that's what we forecasted is more than a financial crisis. So, under normal circumstances, if you would take out 2008 picture, yeah, that will be very painful for us. But – and that's to Jim's point, we managed fixed costs; or to put that differently, our breakeven point in all the factories is significantly lower than it was before. So, we will be able to absorb that volume loss in a much better way than we did in 2008. And that's been the work of the last couple of years.

The other comment I also want to make is yes, the coronavirus as such, yeah, you can call it a black swan event, which came without preannouncement. The recession as such is not a complete shock. And we've been working already the last year on additional cost take-out on balance sheet measures. So, – and that has just allowed us to now ramp up the cost take-out even more so compared to 2008.

And that's – and we started that not just now. We started pretty much some time ago, now we just ramped it up in addition. So, I think the situation is very different. Our preparedness is a little bit different. And our fundamental starting point and breakeven point in factories is very different.

Operator: Your final question comes from the line of Seldon Clarke with Deutsche Bank. Your line is open.

Seldon Clarke
Analyst, Deutsche Bank Securities, Inc.
Q

Hey thanks. Can you just give us a sense of how the cost targets shake out across different regions, and I apologize if I missed this, but did you realize any net cost savings in the first quarter and if so could you just quantify those?

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

A

Yeah, we did realize net cost savings in the first quarter and kind of what we talked about earlier is that just on materials, it was about 1 positive point to our margin in terms of just raw material deflation. And then we had about 0.75 point of additional net cost take-out that we saw within the first quarter.

And then we also reduced some of our marketing and technology expenses as we just put clicked strict controls on some of our discretionary spending. I think as you think about this for the rest of the year, obviously, that rate will ramp up throughout the year. And as you look at it across the globe, we would see it being pretty similar across the globe if you just use revenues to kind of spread it out ratably that way as we are taking cost measures in every part of the world right now, and we're seeing different impacts that we have to offset in every part of the world. But I think that's the best way to think about this.

Seldon Clarke
Analyst, Deutsche Bank Securities, Inc.

Q

Okay, and then just switching gears, obviously, [indiscernible] (1:00:00), but how do you decipher between what's actually a replacement purchase versus new purchase? And how do you kind of determine the state of that appliance that a consumer is replacing? Just trying to think through the consumer's ability or willingness to delay some of these purchases if things are a little bit tighter for longer for consumers?

Marc Robert Bitzer
Chairman & Chief Executive Officer, Whirlpool Corp.

A

Seldon, first of all, we know from, and in different markets from multiple different tracking tools, some external, some internal, you know which consumer purchase is a strict replacement, duress and which one is discretionary which particularly comes as either an upgrade or as part of an entire kitchen. So there's a pretty good data set and that's all pretty comparable.

And we've provided the data also for multiple years and we can give you a little bit more detail behind this one. So we feel pretty good about that number. I think the point which you asked earlier, can replacement purchases be delayed? I would say, to a very limited extent.

And again, that's where you have some experience from 2008, 2009 helps. So a dishwasher which can be replaced or needs to be replaced, yes, then can be delayed. But even in 2008 and 2009, we didn't see these kind of things delayed more than one or two quarters. A washer or refrigerator replacement will not be delayed. We've not seen that in 2008 and 2009, and we don't see that right now. So the vast majority of replacement purchases are hard to delay and will not be delayed by consumers. And we didn't experience that so far.

James Peters
Executive Vice President & Chief Financial Officer, Whirlpool Corp.

A

Yes, and I think even if you look at 2008 and 2009, what we did see is we saw a step-up at times in repairs, which impacts our spare parts business and we saw an increase in that during that time period. Now, I would say today, as we look at that in this time period, it's probably less likely that someone is going to have someone in their home to repair. So it would lead them to lean more to purchasing new rather than repair, like we've seen maybe in some similar downturns.

Marc Robert Bitzer

Chairman & Chief Executive Officer, Whirlpool Corp.

So given that we are at the end of the Q&A sessions and already five minutes over time, let me just wrap up here. First of all, appreciate you all dialing in. Appreciate all your good wishes and also want to echo yours. Stay healthy, stay safe. As you've seen before, it's kind of – it's an environment which none of us have really fully planned for, but it's where we are.

And as painful as the environment is, I feel pretty good about where we are as a company. Q1 was a really – I would really characterize as a demonstration of strong results and resilience in our underlying operations. We all know Q2 will be difficult. We have a perspective on full year, but I think you also heard where we as a company, we're not only prepared to weather this crisis, but we're committed and we're convinced we will come out as a winner out of this crisis.

So with that in mind, looking forward to talk to you either before the next earnings call or latest at next earnings call, and stay healthy.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for your participation. You may now disconnect.