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Whirlpool Corp. (WHR)

Q1 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and welcome to Whirlpool Corporation's First Quarter 2022 Earnings Release Call. Today's call is being recorded.

For opening remarks and introductions, I would like to turn the call over to Senior Director (sic) [Head] (0:17) of Investor Relations, Korey Thomas.

Korey Thomas
Head-Investor Relations, Whirlpool Corp.

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

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

Additionally, price increases or pricing actions referenced throughout this call reflect previously announced cost-based price increases. 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. 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 to 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, Korey. Good morning, everyone. It is my pleasure to discuss the results of our first quarter today and to provide some perspectives for how we intend to continue to transform our business for the better.

Turning to our business. Over the quarter, we worked relentlessly to deliver strong results despite rising cost inflation, supply chain disruption and higher levels of volatility. In fact, this was among the top 10 strongest quarter in the history of our company despite the many external factors that we had to grapple with. We also obviously faced a very tough comparison period from record growth seen last year.

Relative to our performance in 2020, however, we saw a very robust growth. Thanks to the relentless effort of our entire organization, the business remains stronger than where it stood pre-pandemic. Our management team and I have also placed significant emphasis on improving operating margins over the last few years and we remain committed to sustaining the structurally higher profit levels for the future.

To emphasize, we are a structurally stronger Whirlpool than just a few years ago, and this quarter is another reflection of our ability to perform well, even in a tough macroeconomic environment. I'm very confident in the strong fundamentals of the underlying business, and my belief in the go-forward growth remains undented.

Today's guidance change, as you see in our press release, is merely a function of a higher volatility in the environment. We still expect a strong second half and continued robust performance for the remainder of this year. We're exiting the first quarter on strong footing, and our brands are performing very well. That in mind, I'm pleased to announce that we're taking our growth efforts further and are announcing two separate, but highly interconnected initiatives.

First, we're conducting an overall portfolio review that will help us transform the company into a high-growth and high-margin business. Reflective of that, we have also made the decision to embark on a strategic review of the EMEA business. Our EMEA segment has enjoyed solid recovery and turnaround over the past two years despite significant COVID headwinds. Given significant operational improvement in the region, we have decided that now is the right time to conduct the strategic assessment of our long-term value creation in EMEA.

We expect to give you an update with the conclusion of this review by the end of Q3. You will be hearing more from us on this as we continue to grow both organically and evaluate inorganic opportunities in select strategic areas of interest. We are committed to continuing to improve Whirlpool and I couldn't be more confident in the strength of our businesses and brands.

To get into the quarter in more detail, we delivered a solid first quarter with ongoing EPS of $5.31, down by $1.89 versus the all-time record first quarter of last year, but up by 86% against 2020 and up 70% against 2019. This demonstrates that our business is fundamentally stronger than pre-pandemic levels.

We remain confident in the strength of our business and believe that Whirlpool's deliberate actions over the last several years have made us a stronger company today. As our industry and most other industries face historical levels of cost inflation, we've sold over $400 million in the fourth quarter, or approximately a 10% increase on cost of goods sold.

Despite this, we delivered over 9% ongoing EBIT margins and over 16% EBIT margins in our North America business, again demonstrating the earnings strength of the region and the actions we took, transforming margins over the years. We now expect higher levels of inflation to persist throughout the year and have increased our full year cost inflation expectations by $600 million to $1.8 billion.

We also expect a higher price/mix contribution as a result of additional recently announced price increases. We are positioned to deliver strong second half of 2022, exiting the year with actions fully offsetting cost inflation. In other words, there's currently a lag between inflation and pricing, but we expect a catch-up in the second half and remain confident in our actions. However, supply disruptions impacting shipments in the first half of 2022, alongside accelerated cost inflation led us to revise our full year ongoing EPS guidance from $27 to $29 previously but now $24 to $26.

Lastly, with the confidence we have in our business and the strength of our balance sheet, we continue to fund innovation and growth and return cash to shareholders. This includes a 30% year-over-year increase in expected capital investments and a 25% increase in our quarterly dividend. And we are on track to return approximately $1.5 billion in cash to shareholders in the year.

Now I'll turn to our first quarter highlights on slide 5. Again, we demonstrated solid performance during the first quarter delivering ongoing EPS of $5.31 and ongoing EBIT margin of 9.4%. Our successful go-to-market actions in every region partially offset over $400 million of inflation in the quarter. Lastly, we returned a significant level of cash to shareholders with $533 million of buybacks and increased our dividend for the 10th consecutive year.

Turning to slide 6, we show the drivers of our first quarter EBIT margin. As evident, a number of extraordinary items impacted the quarter and we still delivered strong margin. Price/mix delivered 600 basis points of margin expansion led by the successful execution of our pricing actions within each region across the globe, driving positive price mix.

Net cost negatively impacted our margin by 250 basis points, largely driven by increased logistics and energy costs, which were intensified by the Russia-Ukraine conflict.

Additionally, raw material inflation continues to be a significant year-over-year headwind, negatively impacting margin by 700 basis points. Lastly, our strong discipline related to marketing and technology investments positively impacted margin by 50 basis points.

Overall, we're pleased to deliver solid operating margins in what remains a very challenging environment and remain confident in our ability to sustain and grow margins in the future.

Now, I'll turn it over to Joe to review our regional results.

Joseph T. Liotine

President & Chief Operating Officer, Whirlpool Corp.

Thanks, Marc, and good morning, everyone. Turning to slide 8, I'll review results for our North American region. We delivered $2.8 billion of revenue driven by our previously announced cost-based price increases.

First quarter industry shipments represent one of the strongest quarters on record despite being negatively impacted by constrained supply chain, low inventory levels and production disruptions. We believe the industry will ultimately continue to grow beyond these record levels as the fundamental strength of consumer demand trends remains intact.

During the quarter, we experienced increased inflation and operational inefficiencies in addition to the negative impact from temporary volume deleveraging. We delivered at a fundamentally higher level than when we entered the pandemic, sustaining very strong EBIT margins, over 16%, demonstrating the lower fixed cost base of the region. Lastly, our previously announced pricing actions that are coming online in Q2 are on track and position us to fully offset cost inflation as we exit the year.

Turning to slide 9, I'll share more context about demand in the region. Demand remains at sustained strong levels and all indicators point to multiyear growth beyond these levels. Historical growth of approximately 2.5% alone indicate that the industry has yet to fully recover from the great financial crisis with well over 5 million units needed to catch up. This is, in large part, due to the fact that housing remained well below historical and structurally needed levels for over a decade. This is still the case today, which we are seeing play out with housing demand that is constrained by supply.

Next, add the expectation of strong replacement cycles as we compare against a period 10 years ago, when the industry grew at approximately 4%. Then combine this with consumers' higher usage of appliances, which has remained elevated well after consumers have emerged from COVID lockdowns. We see demand as even further room to grow.

In summary, we remain unwavering in our confidence in multiyear demand expansion in North America. We remain equally confident in the strength of our business and its strong brands that serve the needs of millions of consumers daily.

Turning to slide 10, I'll review the results for our Europe, Middle East and Africa region. The region's revenue decline is attributed to negative impact from currency and reduced volume as demand in the region was impacted by the war in Ukraine and the subsequent impact it had on consumer confidence.

Excluding the impact of currency, the region's price/mix actions almost entirely offset the negative impact of demand. For the quarter, the impact from our operations in Russia and Ukraine resulted in an approximate $16 million EBIT decline year-over-year.

At this time, I want to pause and address the war in Ukraine. It is a time of great concern for us all. And it is devastating to see the impact that it's having on the lives of so many people. Our primary focus is the safety and well-being of our colleagues and their communities. And we remain hopeful for a peaceful resolution. We remain supportive of Ukraine and its people. We are proud of the support our teams have provided to refugees. We will continue to support our colleagues through this situation.

In closing, for the overall region, EBIT margin contraction was the result of increased inflation, partially offset by cost-based price increases, including actions that came into effect during March.

Turning to slide 11, I'll review results for our Latin America region. Net sales growth of 4%, driven by cost-based price increases, offsetting expected industry weakness. The region delivered strong EBIT margins of 7.1% despite the current inflationary environment.

Turning to slide 12, I'll review the results of our Asia region. The region's revenue decline is largely attributed to the Whirlpool China divestiture. Excluding this, the region declined by 5% year-over-year.

The region delivered EBIT margins of 4.8%, driven by cost-based pricing actions, offset by lower revenue and inflation. Lastly, COVID-related disruptions and lockdowns in India began to ease, as we exited the quarter.

Now on slide 13, I'll turn it over to Jim to discuss our perspective on 2022.

James W. Peters

Chief Financial Officer & Executive Vice President, Whirlpool Corp.

Thanks, Joe, and good morning, everyone. Now turning to slide 14, I'll review our perspective on the external environment, and what actions we have in place to exit the year with a strong second half.

First, let us address market concerns and misconceptions about demand. Underlying consumer demand remained strong, even with the impact from continued supply constraints and disruptions alongside the spillover effects stemming from greater geopolitical events. We remain very confident that the fundamental strength of consumer demand trends will remain intact over multiple years. With the reorientation towards the home and hybrid work models, the underlying demand strength is here to stay. This is supported as post reopening we continue to see consumers using their appliances at sustained and much higher rates.

Next, historic levels of inflation, notably in raw materials, energy and logistics will impact us throughout the year. However, our previously announced pricing actions are on track and position us to fully offset cost inflation, as we exit the year. Disruptions continue to impact the supply chain and inventories remain at low-levels. But again, we have taken action announcing over $200 million in refrigeration projects, built-in cooking investments driving automation, capacity and innovation, increased capacity in dishwashers to support the strong demand for our products.

In total, we expect to increase our capital investments by 30% year-over-year. We have the right actions in place and are confident in the underlying consumer demand strength.

Now on slide 15, I'll discuss our full year 2022 guidance. We have revised our 2022 full year guidance to reflect the increased inflation we expect to absorb alongside the industry disruptions that we experienced in the first quarter. We now expect 2% to 3% revenue growth and ongoing EBIT margins of approximately 9.5% for the year.

Next, we expect free cash flow of $1.25 billion, or 5.5% of net sales. This represents a full year EPS range of $24 to $26.

Turning to slide 16. We show the drivers of our full year ongoing EBIT margin guidance. We now expect to deliver 725 basis points of price/mix, an increase of 125 basis points, led by additional price increases that have already been announced. Next, we expect net cost takeout to negatively impact margin by 100 basis points, a 50 basis point increase, largely driven by increased logistics and energy costs, partially offset by our ongoing cost reduction initiatives. We now expect our business to be negatively impacted by $1.5 billion to $1.75 billion, or 725 basis points in raw material inflation. This is an increase of 225 basis points led by higher resin and component costs. On a full year basis, raw material inflation is fully offset by our price/mix actions.

Next, as we continue to invest in our business, we expect increased investments of 25 basis points in marketing and technology, and we no longer expect a negative impact from currency. We expect to deliver 55% to 60% of our earnings in the second half as we exit the year with our actions fully in place. We are confident in our ability to, again, navigate a supply-constrained and inflationary environment and deliver approximately 9.5% ongoing EBIT margin.

Turning to slide 17, we show our regional guidance for the year. We have aligned our global growth expectations to reflect the current consumer sentiment in EMEA, along with supply constraints in North America. We expect the North America industry to be approximately flat on a full year basis as the industry recovers in the second half of the year. We remain very confident in the fundamentals of the demand environment for North America, supported by broader home nesting trends and undersupplied housing market and a strong replacement cycle. We remain equally confident in the strength of our business and its brands.

In EMEA, we have reduced our growth expectations to negative 5% to negative 3% as a result of the broader impact from the war in Ukraine. This includes a significant demand reduction in Ukraine and Russia.

Lastly, Latin America and Asia industry expectations remain unchanged from our previous guidance. Regarding our EBIT guidance, our expectation for North America to deliver very strong margins of approximately 16% remains unchanged. In EMEA, we expect margins to recover in the second half to low single-digits, resulting in a full year margin of approximately 0%.

On a full year basis, we expect our EMEA results to be impacted from our operations in Russia and Ukraine by approximately $300 million in revenue. In Latin America, we expect to deliver EBIT margins of approximately 7% as positive price/mix is partially offset by inflation. Lastly, we expect to achieve EBIT margins of approximately 6% in Asia, driven by top line growth, partially offset by inflation.

Turning to slide 18. We will discuss the drivers of our 2022 free cash flow. We have reduced our cash earnings expectation to approximately $2.2 billion due to previously mentioned factors. Our capital investment expectations remain unchanged at $700 million, as we continue to invest in our products and fund organic growth. These investments include unlocking capacity constraints, launching innovative products and furthering our digital transformation journey.

We continue to plan for a moderate inventory build, as we begin to recover our inventory position, particularly in the United States. We anticipate minimal cash outlays related to restructuring or post-integration activities as these have been largely completed. Overall, we expect to deliver free cash flow of $1.25 billion, or approximately 5.5% of sales. Our balance sheet remains very healthy, and we expect this to continue in the future.

Now, let me recap what you've heard over the past few minutes. Our first quarter results demonstrate that we are a different Whirlpool, delivering structurally improved EBIT margins no matter the operating environment. We have the right actions in place to deliver a solid 2022, including our previously announced cost-based price increases of 5% to 18%, addressing inflation across the globe.

Next, the strength in consumer demand trends remains unchanged. The strength of our balance sheet and our strong cash generation expectations provide us with significant optionality. We will continue to invest in the business to support accelerated growth and innovation, while returning approximately $1.5 billion in cash to shareholders. These actions demonstrate the confidence we have in our business and our commitment to drive strong shareholder value.

Now, on slide 19, I will turn it over to Marc to discuss our portfolio transformation, including the strategic review of our EMEA business.

Marc Robert Bitzer

Chairman & Chief Executive Officer, Whirlpool Corp.

Thanks, Jim. Now on slide 20, I will begin with why we are discussing portfolio transformation. Not only during this past quarter, but over past years, we've done a profound assessment of rapid changes in the global macro environment and how our respective global businesses are positioned to win in the future. As we sit here today, we are operating in a very different world than we were just 10 years ago. In short, it is a less global world, where we are experiencing a fundamental global decoupling, which obviously has far-reaching consequences for any global company, a world with rising geopolitical and trade tensions along with global supply chain vulnerabilities and high inflation from freight and logistic costs.

While 10 years ago global scale benefits and the advantages of global asset utilization were significant, we're now experiencing a diminishing advantage of global scale. At the same time, the benefits of regional and local scale become even more compelling and emphasize the strategic importance of leading regional share positions. Put it differently, businesses that are structurally in a weaker position will be more impacted by the unfavorable macro trends than businesses that are in a structurally stronger position.

At the same time, we at Whirlpool have raised the bar for our long-term value creation, which we have announced in October of 2021. We expect our businesses to support 5% to 6% growth, almost doubling our previous value creation growth targets and growing profitably with 11% to 12% EBIT margins and high free cash flow conversion. It is with this value creation criteria that we critically assess all of our businesses.

Now moving to slide 21, I will discuss our overall portfolio transformation. We will accelerate our portfolio transformation towards higher-margin and higher-growth businesses. This will have far-reaching impact on capital allocation or restructuring trends or the absence of them, but also in M&A and potential divestitures. We will achieve success with three strong pillars. One, strengthen and refocus our major appliances business. We will leverage our number one position in North America and Latin America and regional strength across the Americas and prioritize our investments to win in the Americas. At the same time, we will drive our high growth and profitable business in India as penetration rates accelerate growth. In the not too distant future, India will be among the three largest global markets and we are well-positioned to win there.

We will continue to develop and build upon our consumer direct business with leading innovation that transforms consumer experiences and increases engagement with our appliances. We will do this profitably at over 12% EBIT margin, led by the strength of our North America business.

Two, we will grow our small domestic appliance business. This business is more global in nature with both distribution structure in place to continue to grow at an outpaced rate. With the KitchenAid brand, we own the most desired small domestic appliance brand in the world and we will further accelerate our organic growth. At the same time, we're assessing inorganic growth options in pursuit of serving our consumers full cooking journey. With our innovative presence and leading position that dates back to the launch of our iconic KitchenAid stand mixer in 1919, we are positioned to do this by driving portfolio accretive margins of over 15%.

Third, grow our commercial appliance business. Today, this is clearly the smallest of these three pillars, with a healthy commercial laundry business in North America. What makes this segment attractive is the inherent attractive margin profile of more than 15% EBIT, coupled with high level of free cash flow conversion as well as the somewhat countercyclical and stable nature of the business. It also provides opportunities and natural synergies across technology that can be cascaded to our residential business.

The significant progress of our company with four years in a row of all-time record earnings and cash flow has now put us in a position to embark on this portfolio transformation. The opportunity of this transformation would not have been available to us 10 years ago. We have a very disciplined approach to M&A and remain selective to pursue only value-creating acquisitions that make long-term strategic sense for our business.

While I'm the first one to recognize that this is not a short-term transformation and will require hard work, I'm excited and frankly, energized about the path in front of us. We have demonstrated that the Whirlpool of today is very different from a Whirlpool of the past. This will create an even stronger and more valuable company and positions ourselves for the future.

Now I will turn to slide 22 to discuss the strategic review of our EMEA business. This business has undergone significant changes. And in the last two years, we have taken it from a contracting and loss-making business in 2018 to a profitable and growing business in 2021. That structural growth is based on share gains in key countries where we have leading positions in with strong brands our consumers love and higher margins as a result of successfully implemented cost actions and a focus on growth of highly profitable built-in products.

As we look at this business, we do so with both the evolving external landscape including the war in Ukraine and our performance to-date. While we continue to have confidence that this business can achieve attractive EBIT margins, we have to acknowledge that the timeline to achieve these margin levels may take longer than anticipated.

Now continuing to slide 23, I will explain our expectations surrounding any actions we may take. We are assessing the long-term value creation opportunities in EMEA, including the option of continuing ownership as is today. Ultimately, we are reviewing what creates the most value for Whirlpool Corporation and what is required for future success in Europe. Again, to be clear, all options are being assessed. We expect to conclude this review by the end of the third quarter this year.

I will now close my remarks with a few comments. Are we operating in a very dynamic world? Of course, we are. We just delivered another strong first quarter, fundamentally stronger than pre-pandemic levels with actions in place to deliver a strong second half. And we're well positioned with strong, profitable, leading businesses, a balance sheet that provides us optionality and consumers who have never been so engaged with our appliances. We're well prepared to accelerate the focus of our portfolio in high-growth and high-margin businesses, positioning our company for future as a different Whirlpool operating in this very different world.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Susan Maklari from Goldman Sachs. Your line is open.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Thank you. Good morning, everyone.

Joseph T. Liotine
President & Chief Operating Officer, Whirlpool Corp.

A

Good morning, Susan.

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

A

Good morning, Susan.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

My first question is despite all the moving parts and the unexpected events, I mean, obviously, your North America margin was incredibly impressive and certainly well ahead of where we were. And I guess in the spirit of no good deed goes unpunished, despite the 16% this quarter, you left the guidance flat for the year for that region. So can you talk a little bit about how you're thinking of the cadence of that margin as we go through the next several quarters and how we should be thinking about that? And what would potentially drive any upside relative to the guide that you have out there?

Joseph T. Liotine
President & Chief Operating Officer, Whirlpool Corp.

A

Hi Susan. This is Joe Liotine. Yeah, in terms of the North American business, I mean, we feel strong about the consumer demand continues to remain healthy, which is really positive. We feel really good about our value trading go-to-market actions and how we've executed that over a long period of time. And that also is a positive.

In terms of overall margin, we had a lot of different factors playing into there. We did, again, announce price actions that were effective January 1 that helped us mitigate a lot of the cost elements. We are still seeing quite a bit of inflated cost, and we are still seeing quite a bit of disruption in our supply base, kind of limiting our top line growth. And so, on balance, we feel that the approximate 16% EBIT for the year will still be appropriate target for the North American business at this time.

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

A

Susan, it's also, Marc, maybe just to turn your question to positive. The way I look at it, NA had a Q1 margin of 16% – full year 16% guidance. And the same is globally, we're at 9.4% and we're guiding towards 9.5%. So the way I would look at it is right now, we're already on the right run rate, which obviously significantly de-risks our outlook for the year.

Having said that, and to Joe's point, we have further price action already announced, that will help us on the upside. But we all know there's still volatility out there with raw material price, et cetera. So, I think it gives us the appropriate and necessary protection to really deliver the margins which we laid out.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Okay. That's helpful. I do have a follow-up question, but first, just on that, is there anything we should be thinking about in terms of the sequential cadence of the margins in North America as we update the model?

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

A

Susan, it's Marc again. I would – for your model, probably keep it pretty stable. There will always be some pluses and minuses, but it's pretty stable. And again, we feel good about where we had in Q4, Q1, is pretty steady despite all of the moving parts, as you laid out. So I think the team has done a really good job managing towards very stable and sustainable margins.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Okay. And then my follow-up is, obviously, you announced the strategic review of your EMEA operations. Obviously, noting that all options are kind of on the table for you. Can you just give us a bit more detail on how you're thinking about the potential set of opportunities out there?

And I guess within that, we have seen over the last year or so, you do some interesting kind of transactions where you are able to keep the Whirlpool brand in certain regions and kind of financially benefit from that while sort of de-risking the business a bit. So can you talk about whether that's a potential within this? Or, just what are the sort of opportunity sets out there?

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

A

Yeah. Susan, obviously, we announced today, already yesterday, a broader acceleration of our portfolio transformation. So there's, many moving parts. And we're looking at where we can grow organically and inorganically. And obviously, we also announced the strategic review of our European business.

Again, just to reemphasize, in Europe, we've done really good progress over the last two or three years, turning from loss making into a profitable business now where we have been growing. But of course, the question is, as I alluded to earlier, how can Europe fit into our broad portfolio, in particular after we raised the bar for performance.

And so, as such the question is out there, what really delivers the greatest value to Whirlpool Corporation, but also what is the best structural answer to improving our business in Europe. So in that context and I mean it literally, all options are on the table. I referred to retaining the business. We also referred to changing ownership, but there could be also hybrid solutions in between and similar to what you laid out.

So, we're going through a process and again, expect an answer, maybe not a completion, but an answer in terms of what we have in mind and how we will pursue it by the end of Q3.

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

David S. MacGregor
Analyst, Longbow Research LLC

Q

Yes. Good morning, everyone, and I just wanted to ask about the...

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

A

Good morning, David.

David S. MacGregor
Analyst, Longbow Research LLC

Q

Yeah. Good morning. I just wanted to ask additionally on the portfolio transformation. As you transform the portfolio into higher-margin businesses, how much additional capital do you feel you may need to deploy? And can you talk about your targeted ROICs?

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

A

Yes. So David, I mean, first of all, shift – the portfolio transformation can be ultimately driven by – think about resource multiple levels. There is, first of all, the ongoing capital where we put it as a company.

And frankly, we already announced this year, we will invest more in the Americas capacity of new products. As [indiscernible] (00:34:19) is probably going forward, you should – we want to invest less in restructuring, rather put the dollars behind growing business and high-margin business. So let's call it more of a – probably more of an internal shift of resources.

When we talk about external opportunities, obviously, there is no point in there and it's premature to talk about which specific ones, but I would suggest, in general terms refer to a combination of a strong balance sheet and a much stronger underlying earning potential in our company in actual earnings, give us just a lot of optionality in terms of, call it, firepower out there, which is something which we didn't have available to us five or 10 years ago. So it gives us a lot of options in multiple levels.

Having said that, we will stay consistent and mindful in terms of we're not going to overspend. We look very critical at all opportunities out there. But again, between balance sheet and earnings power, our capacity is fairly significant.

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

A

Yeah. And I think, David, a way to think about it also, this is Jim, go forward, is we've always had a pretty consistent level of capital we invest in our business based on the size and all that. And that will continue to be at that type of level. But as we invest in additional businesses, the amount of capital then could remain the same as we're going to invest in some of those.

The other thing you asked on ROIC. Our ROIC targets haven't changed at all. And if you look at some of the portfolio work we're doing, we're obviously looking at [ph] assessing (00:35:43) the future of ones that perform below our target ROIC level. And then as we do acquisitions, go forward and things, obviously, initially, they may not be at that ROIC level, but then as you generate synergies and grow them, that's where we see these are businesses that will contribute to our longer-term increase in ROIC.

David S. MacGregor
Analyst, Longbow Research LLC

Q

Yes. That makes sense. Thanks for that. And then just as a follow-up, can you comment on the opportunities you see in commercial appliances. And I realize you have an existing commercial laundry business that is profitable. And maybe you could size that for us. But do you build a stronger presence in cooking and refrigeration categories? And are you thinking about being just a sort of a really strong niche player? Or do you see Whirlpool eventually holding that leadership position in commercial appliances?

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

A

Well, David, let me again, first of all, repeat why we believe it's an attractive business segment. And again, that's also based on our own experience. It is inherently a very strong margin business. It's a very stable business where it's not only by initial sales it's when the ongoing support for spare parts and kind of fleet sales, if you want to say so, with pretty high cash flow yield. And certain elements are a little bit countercyclical to our residential business. That's why we like this business. That's why we, a couple of years ago, started to acquire small business commercial laundry.

But frankly, it's not only commercial laundry. We have commercial cooking and kitchen segment, as you might know, it's even bigger than the commercial laundry segment. So that will be a business where we would have to grow through acquisitions. Now it is in its nature, it's a little bit more regional, less global than some of the other business, but it's a very attractive one. But it's – again, it's super mature to talk about what we may target for or what not. But as kind of an area where we want to grow, it is actually very high on our priority list.

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

Sam Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

Good morning, Marc, Jim, Joe. I hope each of you are well?

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

A

Good morning, Sam.

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

A

Good morning, Sam.

Sam Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

A couple of questions getting back to the European strategic review. The first – and Marc, we've talked about this obviously, a lot in the past. I think your prior reticence to potentially monetizing the business was that there was a fair amount of shared technology and R&D and clearly managing control of the Whirlpool brand was an issue as well. Has any of that changed specific? I guess what I'm getting at is I know all options are on the table, but realistically, is the sale of the entire business a possibility? Or is it more you're looking to potentially sell off a minority stake and retain some of those assets?

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

A

So Sam, again, I can only repeat all options are on the table, but what you raise are relevant points. But a potential decoupling or partial decoupling of Europe is not a trivial matter. It's technology for brands where I can assure you we would put contracts in places to have either control or indirect control of our brands. So there's limit to how much you really have a clear sale. I mean, there are certain elements, which we want to still keep a certain element of control. Technology is a big one, but also here as we've demonstrated in past, there are solutions in the setup where you can ensure our long-term interests, also our global scale and getting some global synergies and not completely losing them. And these are some of the options which we look at.

Sam Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

And are there any parts of the EMEA business that are higher margin and separable? Or is the business mostly a monolithic type of operation that it would be more of a holistic transaction?

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

A

I would argue, Sam, there's not a lot of pieces, but you can easily just partial of – kind of cut out or whatever. So it is more a one piece of a business. And as such, it's not like you can separate certain individual countries from rest of Europe, because there's a fairly strong connection with supply base and the technology base. So I think you're talking about the overall EMEA regions in a total.

Operator: Your next question comes from the line of Michael Rehaut from JPMorgan. Your line is open.

Michael Rehaut
Analyst, JPMorgan Securities LLC

Q

Thanks. Good morning, everyone. Thanks for taking my questions.

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

A

Good morning, Michael.

Michael Rehaut
Analyst, JPMorgan Securities LLC

Q

First, I just wanted to switch back to the North America segment for a bit. Obviously, with volume, industry volume is down 4%, you guys continue – and your revenue down 8% despite solid positive price/mix. It appears that – or it appears that this quarter, maybe the share losses accelerated a little bit. And obviously, you continue to have challenges with supply chain, but you were probably four to six quarters into these supply chain challenges.

So, I just wanted to get a sense, number one, if I was correct in terms of directionally thinking about the share losses this quarter? And number two, you alluded to some increased investment in the back half and capacity expansions. But how should we think about ultimately resolving this kind of ongoing supply chain – these supply chain challenges that appear to have been the bigger factor in this ongoing issue over the last several quarters?

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

A

So Michael, it's Marc. Let me just address it. First of all, on the demand side, and there's – it may sound like semantics, but I still want to clarify a couple of things. What we see in North America, you referred to the minus 4% demand that is supply. Consumer demand is strong, in fact, very strong. You have a situation where it's very clear, but demand outstrips supply by a wide margin, and that has been going on for several quarters, and that will continue to some extent.

So the underlying demand is very strong, but we – I also really want to refer to this page 9, which we have in the presentation, which just shows you the long-term demand trends. They are strong. Of course, if you compare technically Q1 versus Q1 last year, it's slightly down. Most people lose that, but still up 20% versus 2019 and 2020.

So this demand is strong. We don't see it going away. Replacement is strong and housing will also be strong. So our issue, and we talked about it has been our supply was not capable of catching up or matching the demand side. And even today, we have a fairly sizable number of back orders.

And that ultimately comes back to – throughout the pandemic, North American production was slightly disadvantaged than Asia production. That's as simple as it is. And we are, by a long shot, the biggest producer in North America. We're still – 80% of what we sell in the US is produced in the US.

And that has been through the pandemic a slight disadvantage because there have been less constraints on Asia production. It appears right now the tide started shifting partly because of the COVID wave in Asia. But we are also seeing now a easing of our supply constraints in Q2 whereas this also in combination is we started investing more in capacity, not only in our own capacity but also in our supplier capacity.

So it will not go away magically overnight, but it appears the tide is shifting. So we're actually reasonably confident that we can ramp up our supply. But frankly, it still will remain a volatile environment. So it is just choppy out there. But right now, at least what we're seeing Q2 turns to be better.

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

A

Yeah. And I'd say, Michael, this is Jim. Just to point out as all those things that Marc has mentioned, despite that fact and despite the inefficiencies it's caused us, we're still generating 16% margins within North America.

And so, we are dealing with all the issues and the supply chain constraints, but we're able to manage our business in a way that it's not impacting our margins right now.

Michael Rehaut
Analyst, JPMorgan Securities LLC

Q

Okay. All right. Understood. I appreciate that. I guess just also some – a little bit of further clarity on the portfolio transformation and strategic review of Europe. If you kind of take a step back and look at the various components of what you're trying to achieve from a broader portfolio standpoint.

Obviously, you kind of talked about the fact that your all options are being assessed for EMEA. But as I said before, it's kind of hard to decouple the business or break apart the business in any substantive way. And so, while – obviously, again, you're kind of assessing all options, it does appear that more or less that an outright sale in most elements, maybe retaining some ownership of the Whirlpool brand, maybe some kind of smaller facets of a transaction.

But when you talk about your three pillars and investing in the Americas and India, a higher margin business, it just appears that EMEA, obviously, is the peg that doesn't fit. And so, just trying to make sure that I'm understanding that correctly that in effect it does appear that a large sale or – of most of the assets at least will – to us at least what it sounds like you're saying.

And number two, though, in terms of the reinvestment of the proceeds from such a transaction how should we think about that? Should it be more share repurchase? Is there going to be an element of reinvestment you highlighted inorganic growth opportunities, just trying to think of the different redeployment of any proceeds?

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

Michael, first of all, with regards to Europe, I would not yet jump to any conclusion about what is more realistic or less realistic. So what I said earlier, the decoupling is not trivial, but it's doable.

And of course, it's easy to have a trusted partner on the other side of a transaction when it's a lot easier, but it's doable. So yes, an outright sale is possible. It's one of the options which we look at, and then we will go from an objective assessment about all the pros and cons, which again also include retaining the business.

That's in a certain way a baseline. And we got to assess our own opportunities and how we drive margin to required levels and need to compare with how does it stack up to some other options. But so, at this point, I really would not exclude any of the options which we look at.

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

Yeah. And I'd say, Michael, on your question on the proceeds in that, again, we're very early in the process, but I think this doesn't change our capital allocation strategy right now.

And if you look at – we've been focused, obviously, on returning cash to shareholders. But as Marc talked about earlier, and even we've talked about this recently with the strength of our balance sheet now, we are looking at inorganic growth opportunities.

And so those two are going to be part of the capital allocation strategy and balance, but it doesn't change the priorities that we have. It just over time, gives us more to invest in higher growth or potential high-growth areas of our business.

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

Eric Bosshard
Analyst, Cleveland Research Co. LLC
Q

Thank you. Good morning.

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

Good morning.

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

A

Hey, Eric.

Eric Bosshard
Analyst, Cleveland Research Co. LLC

Q

Hi. A question and then a follow-up. First of all, relative to 90 days ago, just to separate consumer demand and shipments, trying to figure out what looks different. The industry shipment number, you took down from up 2% or 3% to flat. And so trying to figure out what changed that caused you to revise that? And then secondly, it sounds like while that's changed, you haven't seen anything different with consumer demand. But I just – I wanted to understand that with greater clarity if that's indeed the case.

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

A

Eric, I can take it. I think the biggest change, which we see and which has been reflected in forecast. In Q1, the supply was shorter than we had in mind and [ph] probably (00:48:39) the entire industry had in mind. So that's why I would put the Q1 industry shipment number entirely down to supply chain constraints. We know our own numbers, and we know – I mean, obviously, we can read what the rest of the industry does. So because we don't think the supply will catch up what we lost in Q1 throughout the rest of the year, that's what you see reflected there. But the way to look at this zero percent full year guidance basically means, yeah, we're planning for roughly 3% growth – industry growth for rest of the year.

Eric Bosshard
Analyst, Cleveland Research Co. LLC

Q

Okay. And then secondly, within the guidance, you lowered the industry shipment numbers. You've raised the raw material number, your performance versus the industry is a bit wider than it was and yet the margin guidance is held. And so what is better within the business or within profitability to offset these two or three other things that are worse?

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

A

Yeah. I'd say, Eric, and if you – this is Jim. If you take a look at it, we did reduce the margin guidance slightly to the 9.5%. But the biggest thing that offsets this significant increase in materials is the additional pricing that we announced within the first quarter, and that we'll now see running in throughout the second and the third quarter for our business. And so that's as we talked about earlier, as we've seen higher material costs, we continue to take cost-based price increases to offset that.

And it's just a matter of the timing for the year and it's why we reduced the margin down slightly to reflect that that our pricing is now catching up with some of the cost increases we've seen. And it's not just on materials, obviously. It's also been on things such as logistics costs and energy costs that were all significantly higher and have accelerated at a rate greater than we originally thought they would this year.

Operator: Your next question comes from the line of Liz Suzuki from Bank of America. Your line is open.

Elizabeth L. Suzuki
Analyst, BofA Securities, Inc.

Q

Great. Thank you. So SG&A had been running above $500 million per quarter for the last six quarters and dropped pretty sharply in the first quarter and as a percent of sales, it's the lowest it's been in decades. I mean how much of that reduction in SG&A was the result of transitory factors like the temporary layoff of plant workers in Clyde? Or in other words, how much of that reduction is sustainable and how much cost is expected to come back in as supply constraints and production issues ease?

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

A

Yeah, Liz. This is Jim. And I think if you step back and take a look at it, partially, there is a benefit in there from currency translation as we translate everything into dollars from around the globe that has helped us reduce that. Two, we – in our walk, we talk about marketing and technology investments, which were lower year-over-year within this quarter, but then we expect to invest more in the back half of the year. So that's another big driver.

The third thing is, we had a business in China last year that also had a significant amount of SG&A in it. And that's now structurally out of there because we don't consolidate that business anymore. We've got some ongoing cost reductions that continue to benefit us in there, and we've talked about those in the past, but we see the full run rate of those coming in, in this year.

And then, we have some smaller moving parts that can be things such as a small gain on a property sale, but then offset partially by increases in bad debt reserves in places like the Ukraine. So, there's a lot of factors in there, but I think you have to look at that and say at least half of that plus is probably what I would say is a structural run rate reduction and the other is just maybe timing of things, as I said, like marketing and technology investments.

Elizabeth L. Suzuki
Analyst, BofA Securities, Inc.

Q

Okay. That's really helpful. And then, a follow-up question is just about the – if there's 2022 price increases are able to catch up to inflation by the second half? Could there be some favorable flow-through from pricing versus inflation in 2023 that we should be considering?

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

A

This is Marc. The current environment is so volatile, but to be honest, there's a lot of moving parts which will happen before now in 2023. But having said that, with all the actions which we have right now put in place, particularly on the pricing side, but also what we do on supply side. Absent of further massive volatility shocks on the raw material side, I think we will have very strong exit run rates coming out of Q4, which, by definition, should spill over then in 2023.

But again, the caution I have right now, even entering the first quarter, we didn't have a war on our radar screen. And so, this is a very dynamic, to put it mildly, environment, and we've just got to be prepared for everything. But having said that, absent of major shocks, we will have very, very strong exit run rates.

Operator: Your next question comes from the line of Dan Oppenheim from Credit Suisse. Your line is open.

Dan Oppenheim
Analyst, Credit Suisse Securities (USA) LLC

Q

Great. Thanks very much and thanks for taking the call. Just wondering in terms of the supply difficulty that you've spoken about initially, there's a talk in terms of the 30% increase in CapEx over the course of the year, later you talked about the sort of some of the issues easing and shifting here in the second quarter.

Just trying to get a better sense in terms of how meaningful that is in terms of what you're saying with the easing or if we should think about that as more sort of being bit later in the year in terms of significant progress on that, and then sort of benefiting then as the CapEx comes through?

Joseph T. Liotine
President & Chief Operating Officer, Whirlpool Corp.

A

Yeah, Dan, this is Joe Liotine. So we did talk about how March performed a little better, and we expect that kind of ramp continue into Q2. It's going to be a slight improvement in Q2, and then a bit more meaningful improvements into Q3 and Q4. There's a lot of factors in here, but we've seen already indications that give us a bit of optimism and then we've seen some actual performance that's slightly better. And so that combination kind of sets forth a Q2 that's going to have improvement, but really the bigger ramp happens in Q3 and Q4 with an exit rate in Q4 that shows us kind of the opportunity to get growth back and share back that we have been discussing.

Dan Oppenheim
Analyst, Credit Suisse Securities (USA) LLC

Q

Great. And then secondly, just wondering about [ph] when it comes to (00:54:53) the free cash flow for the year, how to think about inventory levels over the course of this year? And just what – overall what goes into that in terms of investment?

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

A

Yeah, Dan. And this is Jim. I think as we pointed out that as we go throughout the year, we do expect to build inventories slightly as we begin to see later in the year some recovery in certain areas of our supply chain, but it shouldn't be significant for the year. And what we're guiding to out there right now, is about a $200 million increase year-over-year in working capital.

And the biggest portion of that will be, as I mentioned, in inventories. We just try and get our level of stock within our own logistics network to a healthy level, as we begin to fulfill some of the backlog of orders, so the next step is for us to continue to increase the health of our own supply chain.

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

Christopher Kalata
Analyst, RBC Capital Markets LLC

Q

Hi, this is actually Chris Kalata on for Mike. Thanks for taking our questions. So my first question is, I was hoping you could give us an update on the current state of your Russian operations today. And is maintaining a presence there going to complicate any potential EMEA divestitures in the future?

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

A

Yeah. I can take this one. So we – as we published, we have a local-for-local production in Russia, which historically satisfied about 80% or 90% of our volumes in Russia.

We are not importing goods from our European sites into Russia, but we maintain a very low level of production, basically keeping the lights on in our Russia factory. Is that sustainable over time? It's probably not.

But right now, we keep it running to a certain volume, of course, fully compliant with all sanctions and everything else. I want to point out Russia is not the reason why we look at the strategic review in Europe.

Russia has been a good and important market for Europe, but that's not the reason why we look at the strategic review. It's a number of factor in the broader equation in the long-term landscape and us, like many other companies will, of course, carefully consider what strategically is possible or not possible in Russia going forward.

Christopher Kalata
Analyst, RBC Capital Markets LLC

Q

Understood. And just turning back to your demand outlook in North America, you're expecting demand to remain strong in the second half, even though leading housing indicators are starting to decelerate and clearly there's more uncertainty around demand going forward. So I want to get your sense on rationale for this and confidence around making that assumption at this point.

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

A

It's Marc. In all honesty, I don't see where you see the uncertainty of demand. I said earlier that demand clearly and has for the last two years outstripped supply by a wide margin.

Replacement is as strong as ever and the COVID pandemic and now also the more and more hybrid work models will further accelerate replacement because you basically have a higher usage of appliance. And we still see that confirmed even two years into the pandemic.

So, our outlook on the fundamental long-term consumer trends in North America, are as bullish as we've ever been. So honestly, I just don't see that slowing down. Also on the housing side, I know we're just talking about mortgages.

If you look at the fundamental demographic trends, the age of the housing stock, the demand out there, I wouldn't bet against US housing. And we're certainly very optimistic about the long-term US housing trends.

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

Okay. So with that, it looks like we're coming to the end of the Q&A session. So first of all, thank you all for joining us today. As you've just seen and heard, with Q1, we feel very good about, very solid Q1.

Obviously, a lot of moving parts, as some of you pointed out in the quarter and the environment around us, but I think we've demonstrated yet again, we can deal with a lot of challenges.

I think we have put all the right actions in place to have a very, very strong second half. And as it comes to the portfolio transformation, we will keep you updated. In particular, once we come to the earnings call after the third quarter.

With that in mind, thanks again for joining us, and have a wonderful day.

Operator: Ladies and gentlemen, that concludes today's conference call. You may now disconnect.