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Compass Diversified NYSE:CODI

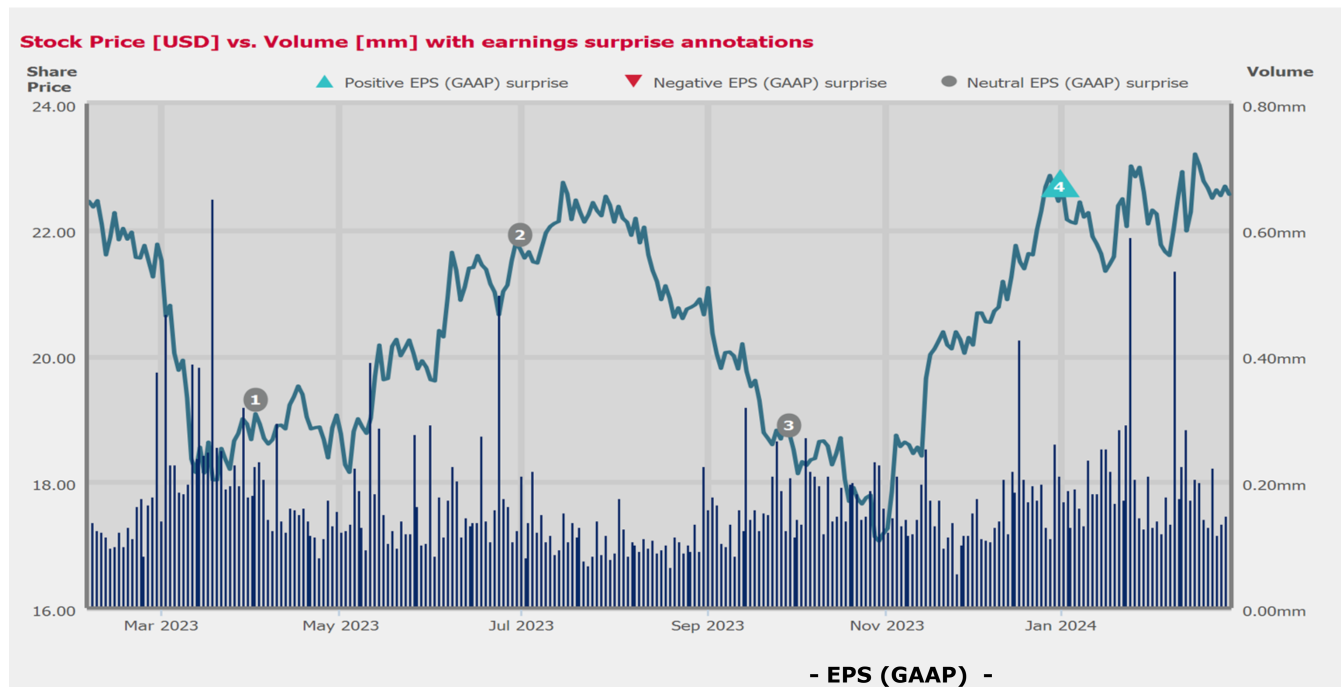
FQ4 2023 Earnings Call Transcripts

Wednesday, February 28, 2024 10:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2023-			-FQ1 2024-	-FY 2023-			-FY 2024-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS (GAAP)	0.03	-	-	0.06	1.01	2.46	▲143.56	0.30
Revenue (mm)	576.55	566.99	▼(1.66 %)	547.12	2209.20	2058.88	▼(6.80 %)	2327.85

Currency: USD
Consensus as of Jan-24-2024 2:40 PM GMT



- EPS (GAAP) -	CONSENSUS	ACTUAL	SURPRISE
FQ1 2023	(0.02)	1.46	NM
FQ2 2023	0.19	0.19	(1) 0.00 %
FQ3 2023	0.20	(0.33)	NM
FQ4 2023	0.03	-	-

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Call Participants

EXECUTIVES

Elias Joseph Sabo
Partner & CEO

Patrick A. Maciariello
Partner & COO

Ryan J. Faulkingham
Executive VP, CFO & Co-Compliance Officer

ANALYSTS

Kyle Joseph
Jefferies LLC, Research Division

Lawrence Scott Solow
CJS Securities, Inc.

Mark Feldman
William Blair & Company L.L.C., Research Division

Michael David Zabran
ROTH MKM Partners, LLC, Research Division

Robert James Dodd
Raymond James & Associates, Inc., Research Division

ATTENDEES

Cody Slach
Gateway Group, Inc.

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Presentation

Operator

Good afternoon, and welcome to Compass Diversified's Fourth Quarter and Full Year 2023 Conference Call. Today's call is being recorded. [Operator Instructions].

At this time, I would like to turn the conference over to Cody Slach of Gateway Group for introductions and the reading of the safe harbor statement. Please go ahead, sir.

Cody Slach
Gateway Group, Inc.

Thank you, and welcome to Compass Diversified's Fourth Quarter and Full Year 2023 Conference Call. Representing the company today are Elias Sabo, CODI's CEO; Ryan Faulkingham, CODI's CFO; and Pat Maciariello, COO of Compass Group Management.

Before we begin, I'd like to point out that the Q4 2023 press release, including the financial tables and non-GAAP financial measure reconciliations for subsidiary adjusted EBITDA, adjusted EBITDA, adjusted earnings and pro forma net sales are available at the Investor Relations section on the company's website at compassdiversified.com.

The company also filed its Form 10-K with the SEC today after the market closed, which includes reconciliations of certain non-GAAP financial measures discussed on this call and is also available at the Investor Relations section of the company's website. Please note that references to EBITDA in the following discussions refer to adjusted EBITDA as reconciled to net income or loss from continuing operations in the company's financial filings.

The company does not provide a reconciliation of its full year expected 2024 adjusted earnings, adjusted EBITDA or subsidiary adjusted EBITDA because certain significant reconciling information is not available without unreasonable efforts. Throughout this call, we will refer to Compass Diversified as CODI or the company. Now allow me to read the following safe harbor statement.

During this call, we may make certain forward-looking statements including statements with regard to the expectations related to the future performance of CODI and its subsidiaries, the impact and expected timing of acquisitions and divestitures and future operational plans such as ESG initiatives. Words such as believes, expects, anticipates, plans, projects, should, and future or similar expressions are intended to identify forward-looking statements. These forward-looking statements are subject to the inherent uncertainties in predicting future results and conditions.

Certain factors could cause actual results to differ on a material basis from those projected in these forward-looking statements, and some of these factors are enumerated in the risk factor discussion in the Form 10-K as filed with the SEC for the year ended December 31, 2023, as well as in other SEC filings. In particular, the domestic and global economic environment, supply chain, labor disruptions, inflation and rising interest rates all may have a significant impact on CODI and our subsidiary companies. Except as required by law, CODI undertakes no obligation to publicly update or revise any forward-looking statements, whether because of new information, future events or otherwise.

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

Elias Joseph Sabo
Partner & CEO

Good afternoon, everyone, and thanks for joining us today. I'm pleased to report a strong fourth quarter, capping off another exceptional year for CODI. Our results continue to demonstrate that owning premium businesses with defensible competitive moats can drive financial outperformance, even during periods of economic uncertainty. These results are highly intentional.

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In 2018, we embarked on a strategy to own and manage high-growth, innovative and disruptive businesses. This transformation is driving a significant tailwind for our business as evidenced by our fourth quarter. Despite experiencing unique challenges in our business, 2023 marked our fifth straight year of subsidiary adjusted EBITDA growth. Our branded consumer businesses produced essentially flat pro forma subsidiary adjusted EBITDA results compared to prior year.

On the other hand, our industrial businesses produced 18% annual growth in subsidiary adjusted EBITDA. Our diversification, yet again, led to a reduction of financial volatility, which we believe will be further reduced as we add more subsidiaries and enter into the health care vertical. In our branded consumer vertical, inventory destocking issues masked the underlying strength of most of the brands we own throughout 2023. Lugano once again delivered remarkable growth producing 53% annual revenue growth and 65% adjusted EBITDA growth.

As we have repeatedly mentioned, Lugano has created a very innovative and disruptive business model within the high jewelry industry. We continue to fund capital investment to expand the company's footprint and inventory position, realizing exceptionally strong returns on invested capital that is fueling the company's rapid growth.

In the fourth quarter, our branded consumer businesses experienced strong subsidiary adjusted EBITDA growth of 26% over prior year as inventory destocking headwinds started to subside. You will remember the prior year's fourth quarter started a major inventory destocking trend that lasted throughout 2023. We believe channel inventory will continue to rightsize and turn into a tailwind in 2024, which we expect will enable a much higher level of growth for many of our consumer businesses, making up for the growth we didn't experience in 2023.

Our industrial businesses generated double-digit subsidiary adjusted EBITDA growth in the fourth quarter and full year. The easing of inflationary pressures boosted margins and resulted in adjusted EBITDA growth above long-term trends. We expect this tailwind to normalize as we progress through 2024 and for our Industrial vertical to revert back towards trend growth. We remain optimistic about our industrial vertical in 2024 since backlogs remain at very healthy levels.

Now I'd like to return to our competitive positioning. The strategy we outlined at last month's Investor Day detailed our focus on buying and managing more innovative and disruptive businesses. We unveiled this strategy with our management change in 2018. Since then, we have been opportunistically divesting our subsidiaries that grew alongside their industry and focused our efforts towards acquiring more innovative and disruptive businesses with fundamentally faster growth rates. We've seen the efforts of this transition really begin to manifest in the numbers as evidenced by our results in the fourth quarter and full year.

This important shift has boosted the power of our growth engine to produce a more consistent faster level of growth. So when 1 or 2 of our subsidiaries aren't growing near trend, for example, what we experienced in 2023 with both BOA and PrimaLoft, we have other subsidiaries growing at or above trend, like Lugano and our industrial vertical did in 2023. This diversification in growth drivers not only reduces financial volatility, but it also increases the likelihood of us achieving our core growth rate on an annual basis.

As we outlined at our Investor Day, another way in which we create value for our shareholders is through opportunistic M&A transactions. Although the M&A markets were weak for most of 2023, we were able to consummate the divestiture of Marucci Sports, realizing a significant gain for our shareholders. In early 2024, we acquired The Honey Pot company, an innovative, disruptive company in the feminine hygiene space. We believe opportunistic M&A transactions like Marucci and Honey Pot create value for our shareholders, accelerate our core growth rate and minimize the likelihood of long-term growth decay on a consolidated basis.

Before passing the call over to Pat, I'd like to discuss 2 topics. First, a few macro trends we're seeing and second, address the shift to the way we guide our business, which we believe will simplify how you think about evaluating CODI. First, a few thoughts on how macroeconomic conditions are affecting our business. Including The Honey Pot Company, approximately 70% of our consolidated subsidiary adjusted EBITDA is generated by our branded consumer vertical.

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So far in 2024, the U.S. consumer is looking healthy, notwithstanding tighter monetary conditions that have existed over the past 2 years. Unemployment continues to be at historically low levels. Wages continue to grow above trend, and the easing of inflationary pressures is causing real wages to grow again after declining for much of the past 2 years. [Excess] savings continue to exist from pandemic-led government transfer payments albeit at lower levels as savings buffered high inflation rates over the past couple of years. Taken together, we believe this bodes well for our branded consumer business in 2024.

Regarding our industrial vertical, which represented approximately 30% of consolidated subsidiary adjusted EBITDA in 2023, global growth is expected to remain positive, but at subdued levels due to the negative impact of tight monetary conditions and global tensions. We believe our industrial subsidiaries are positioned to continue to take market share through innovation, as evidenced by Outdoor Solutions being first to market with a biodegradable solution and Arnold Technologies leading the market in advanced materials used to generate green energy.

We believe our industrial businesses will continue to perform well again in 2024 as a stable macro economy and company-led innovation is expected to lead to another year of growth. Thus far in 2024, our results have exceeded our expectations. While we are reiterating our outlook we provided just a few weeks ago at our Investor Day, we are certainly optimistic about 2024 and believe upside exists based on the trends we are currently experiencing.

Speaking of our outlook, we are adjusting how we communicate our guidance to help simplify the analysis of our business. Today, we currently own 10 subsidiary businesses across the consumer and industrial verticals. And at some point, we expect to enter the health care market. We expect to own and manage 15 companies one day and perhaps more than that in the future. To help quantify this scale more simply, we will provide subsidiary adjusted EBITDA guidance ranges on a branded consumer and industrial level.

Despite this change, as part of our governance protocols, we remain focused on transparency, and we will continue to disclose the same level of detail as we have done previously. We are shifting the narrative as we believe it will be easier for you to follow CODI as we continue to expand the number of subsidiaries we own.

With that, I will now turn the call over to Pat.

Patrick A. Maciariello
Partner & COO

Thanks, Elias. As a reminder, throughout this presentation when we discuss pro forma results, it will be as if we own PrimaLoft as of January 1, 2022. In addition, we have not included The Honey Pot in our 2023 results as it was acquired after year-end.

I'm pleased to report on a very successful year for CODI in 2023, one in which we exited the year far stronger than we entered, thanks to the quality and positioning of our businesses. On a consolidated basis for the year, revenue was approximately flat and pro forma subsidiary adjusted EBITDA grew by 4.4%. As Elias mentioned, in the fourth quarter, on a consolidated basis, we saw material acceleration as many of the headwinds facing our businesses over the last year began to abate.

As a result, in the fourth quarter, revenue and subsidiary adjusted EBITDA growth exceeded our expectations, growing by 7% and 27.4%, respectively. Both our industrial and branded consumer verticals had strong quarters, growing subsidiary adjusted EBITDA by 30.2% and 26.3%, respectively.

For the full year, within our industrial vertical, revenues decreased by 5.1% and subsidiary adjusted EBITDA increased by 18.3% versus 2022. In this quarter, we saw broad earnings strength in our industrial businesses as positive revenue mix to higher-margin products, combined with lower input and shipping costs. In many cases, we passed on the benefits from lower cost to our customers, leading to the slight revenue decline. However, our industrial management teams continue to operate efficiently and drive solid margin growth.

For the year, both Arnold and Outdoor grew adjusted EBITDA by over 20% and Sterno by over 11%. A continued return to travel and more pre-pandemic activities continues to have a positive impact on

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several areas of our industrial business and we believe this trend will be ongoing. In addition, specifically at Arnold, we want to once again point out the investments in research and development made over the last several years. As a result of Arnold's Technology Center, the team continues to add new products -- projects. And, though not a significant driver of growth in 2023, the company is growing rapidly in new industries, including medical devices.

Turning to our consumer vertical. For 2023, revenues increased by 2.7% and pro forma subsidiary adjusted EBITDA was approximately flat versus 2022. Growth accelerated in the back half of the year, however, and for the fourth quarter, revenue and subsidiary adjusted EBITDA grew by 13.4% and 26.3%, respectively, for Q4 2022. As Elias mentioned, we believe this quarter represents a transitional period where -- though inventory-related distortions in the supply chain have not fully dissipated, the headwind they have had on our consumer revenues has weakened significantly.

Specifically, to give color on 2 of our businesses further up the supply chain, though challenges at PrimaLoft remain, they appear to be abating somewhat, and we are seeing improvements. Brand partners are delaying the timing of their orders often to the latest possible moment, but many indicate solid order expectations on a full year basis. Conversely, BOA Technologies returned to growth in adjusted EBITDA in the quarter, and we are further encouraged by double-digit growth in bookings thus far in 2024.

Lugano once again led our growth for the quarter and for the year as both revenue and adjusted EBITDA grew by 53% and close to 65%, respectively. We grew revenue in every salon in 2023 and saw meaningful increases in average transaction value. In addition, in the fourth quarter, we benefited from the relocation and expansion of our flagship Palm Beach salon. We are excited about the opening of our London salon in the second quarter of this year and continue to evaluate additional markets.

As a whole, we are very pleased with the performance of our subsidiary businesses in 2023 and in particularly in the fourth quarter. We are confident in the positioning of our businesses and the outlook for 2024.

I will now turn the call over to Ryan for additional comments on our financial results.

Ryan J. Faulkingham
Executive VP, CFO & Co-Compliance Officer

Thank you, Pat. Moving to our consolidated financial results for the quarter ended December 31, 2023, I will limit my comments largely to the overall results for CODI since the individual subsidiary results are detailed in our Form 10-K that was filed with the SEC earlier today.

As a reminder, our sale of Marucci occurred in the fourth quarter of 2023 and its results have been reclassified to discontinued operations for all periods. On a consolidated basis, revenue for the quarter ended December 31, 2023 was $567 million, up 7% compared to $529.7 million for the prior year period. This increase was primarily a result of strong growth at Lugano and 5.11, partially offset by lower revenue at Sterno, Altor and Velocity.

Consolidated net income for the fourth quarter was $139.4 million compared to a net loss of $11.8 million in the prior year. The fourth quarter net income was primarily due to the gain on the sale of Marucci, partially offset by impairment expense recorded at PrimaLoft. Adjusted EBITDA in the fourth quarter was $94.8 million, up 35% compared to $79 million in the prior year. The increase was due to strong growth at Lugano and 5.11 as well as an expansion in EBITDA margin at our industrial businesses. Included in adjusted EBITDA in the fourth quarters of 2023 and 2022 were management fees and corporate costs of $20.9 million and $20.8 million, respectively.

Adjusted earnings for the fourth quarter were significantly above our expectations, coming in at $38.1 million. This was up significantly from $16.3 million in the prior year quarter and up 29% sequentially. Adjusted earnings was above our expectations due to strong performances at Lugano and 5.11 and by our industrial businesses. In addition, our adjusted earnings was positively impacted throughout 2023 by much lower taxes than we anticipated at our subsidiaries, primarily Velocity and PrimaLoft where we had weaker performance and related income tax benefits.

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We believe that for modeling purposes, the tax provision at our subsidiaries on a consolidated basis will approximate 10% of subsidiary adjusted EBITDA. However, in 2023, our tax provision was only 7% of subsidiary adjusted EBITDA.

Now on to our financial outlook. At our Investor Day in January, we mentioned that we would be enhancing our guidance to the Street to reduce confusion. Providing guidance on our adjusted earnings and subsidiary adjusted EBITDA will continue and remain the same. However, we are adding a third guidance metric called adjusted EBITDA. This differs from subsidiary adjusted EBITDA in that we deduct corporate level expenses and corporate level management fees.

One additional note, we will refer to subsidiary adjusted EBITDA on a pro forma basis upon acquisitions, but we will not provide adjusted EBITDA nor adjusted earnings on a pro forma basis. We are also enhancing guidance by providing subsidiary adjusted EBITDA separately for our consumer and industrial verticals, as Elias previously mentioned.

So now moving to our 2024 guidance. As a reminder, we acquired The Honey Pot Company on February 1 of this year. We expect full year 2024 subsidiary adjusted EBITDA, consistent with the range we provided at our Investor Day of between $480 million and $520 million. The midpoint of this range, $500 million implies an 11% growth rate over 2023. This is pro forma for the acquisition of The Honey Pot. The subsidiary adjusted EBITDA range for our industrial businesses will be between $125 million and $135 million. The subsidiary adjusted EBITDA range for our branded consumer businesses will be between $355 million and $385 million.

Moving to our new adjusted EBITDA guidance, we expect full year 2024 adjusted EBITDA to be between $390 million and $430 million. This range factors in an expected $86 million of corporate level overhead and management fees in 2024. This compares to $341 million in adjusted EBITDA in 2023.

Now on to adjusted earnings. We expect full year 2024 adjusted earnings to be between $145 million and $160 million. At the midpoint of this range and assuming the same share count as at December 31, 2023 of 75.3 million shares, we expect to earn $2.03 in adjusted earnings per common share. Given the discontinued operations in 2023, it's challenging to compare 2024 adjusted earnings to 2023 adjusted earnings. However, as I mentioned earlier, last year's adjusted earnings benefited by approximately $13 million from lower taxes at our subsidiaries than we had anticipated.

Turning to our balance sheet. As of December 31, 2023, we had approximately $450.5 million in cash, approximately $598 million available on our revolver and our leverage was 3.11x. During the fourth quarter, we sold Marucci, providing approximately $480 million in cash at closing. We also sold 3.5 million common Trust shares in a private placement, yielding approximately $74 million in cash proceeds. Subsequent to the end of the fourth quarter, we acquired The Honey Pot Company for an enterprise value of $380 million.

We used cash on our balance sheet to fund our $343 million investment with the remainder of the purchase price provided by minority shareholders. After closing The Honey Pot acquisition, our total leverage increased to approximately 3.7x. As a reminder, the first and second quarter are traditionally our lower cash flow quarters. In addition, we prefunded Lugano with significant inventory early in the first quarter of 2024 in preparation for the London salon opening, which is planned in the second quarter, and thus, we anticipate our leverage will increase during the first and second quarter.

Then declined sequentially in the third and fourth quarter as a result of strong growth we expect in our subsidiary adjusted EBITDA. We have substantial liquidity. And as previously communicated, we have the ability to upsize our revolver capacity by an additional $250 million. With our liquidity and capital, we stand ready and able to provide our subsidiaries with the financial support they need, invest in subsidiary growth opportunities and act on compelling acquisition opportunities as they present themselves.

Turning now to cash flow provided by operations. During the fourth quarter of 2023, we received $21.1 million of cash flow from operations, primarily due to strong operating performance. This is up $10 million from the prior year's comparable period. During the fourth quarter, we used $24.4 million in working

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capital, a decrease from use of $27.7 million in the prior year. For the full year 2023 period, cash flow provided by operations increased $106 million as compared to the prior year.

During 2023, Lugano invested $157 million in inventory to fund its growth. This inventory investment has generated an exceptional return on invested capital and enabled the strong growth Lugano has experienced. Outside of Lugano, our remaining subsidiaries monetized significant working capital during 2023.

And finally, turning to capital expenditures. During the fourth quarter of 2023, we incurred $17.2 million of capital expenditures at our existing subsidiaries compared to $23.7 million in the prior year period. The decrease was primarily a result of the timing of retail build-outs at Lugano to support their continued growth.

For the full year of 2024, we anticipate total CapEx of between $50 million and $60 million. We continue to see strong returns on invested capital at several of our growth subsidiaries and believe they will have short payback periods. Capital expenditures in 2024 will primarily be at Lugano for new retail salons.

With that, I'll now turn the call back over to Elias.

Elias Joseph Sabo
Partner & CEO

Thank you, Ryan. I would like to close by briefly providing an update on the M&A market and our strategic initiatives. In the fourth quarter, we not only saw an increase in deal activity, but also in the quality of businesses coming to market. Our competitors continue to struggle with leverage buyout financing as a function of the current environment, specifically in consumer. We are seeing our cost of capital advantage significantly expand in this environment which leads us to believe that now is a great time for us to be an acquirer.

Our acquisition of The Honey Pot Company in February is a perfect example. Our competitors in the consumer market pulled back dramatically just as their financing partners have, which is how we were able to get this deal done. For an on-trend company in the personal health and well-being space, we were able to transact at a multiple that was lower than the historic average. Today's market reminds us that the financing market of 2020 when large uncertainties driven by COVID competition sideline, yet our permanent capital structure allowed us to buy quality assets like Marucci and BOA.

Today, we have a level of optimism that we haven't had in years. We're able to consummate M&A at more attractive valuation with better shareholder return prospects than in past years. On the ESG front, our focus continues to not only be about compliance, but ESG is integral to our mission, reflecting our commitment to transparency and responsible business practices. This focus is essential for our continued success and the creation of long-term value for our investors and stakeholders.

We will release our first sustainability report in Q2 which we expect to include details of our greenhouse gas emissions, human capital initiatives and governance practices. Additionally, we will continue to seek partnerships and acquisitions that align with our sustainability values, ensuring that our growth is both responsible and aligned with our long-term vision.

Our most recent acquisition of The Honey Pot exemplifies the type of company that aligns with CODI's strategic vision and objectives. To conclude, we continue to make great strides improving upon the quality of our subsidiaries as a whole. In addition, we remain steadfast in our efforts to identify and acquire similar disruptive businesses to further build upon our track record of delivering growth for our shareholders.
I'd like to thank the entire CODI team for their tireless efforts in transitioning this business into a different and stronger company than we were 6 years ago. With that, Operator, please open the lines for Q&A.

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Question and Answer

Operator

[Operator Instructions] Your first question comes from Larry Solow of CJS Securities.

Lawrence Scott Solow
CJS Securities, Inc.

Great. I guess first question on -- maybe I'll ask, just on the acquisition environment. It sounds like as you expressed last month, too, gotten a lot better and it kind of fits right into your sweet spot. I'm just curious with your leverage is going to be sounds like around 4x during the first half of the year at least. What's your ability to acquire larger sized assets? Would you be going to go up to 5x plus? Or how do you look at that? And maybe would you might entertain the idea of selling some of your smaller subsidiaries?

Elias Joseph Sabo
Partner & CEO

Yes, Larry, I would say -- and thank you for the question, and good afternoon. I would say the acquisition market is better. I don't know that I'd refer to it as a lot better. It's clearly in 2021 when we were seeing deals kind of at a very high level and some good quality companies that were coming. But compared to '22 and '23, we often say it's hard to fall off the floor. And I think '23 sort of kind of represented the floor. So it's clearly a pickup.

And not only are we seeing a pickup in the number of deals, but we're also seeing some quality companies come through as well. So that bodes well. Regarding your question, I think, right now we're at 3.7x leverage. It's a little bit outside of our kind of leverage window as Ryan mentioned in his commentary, it could float up a little bit. It's not going to be a material floating up in the beginning of the first half of the year. And then it will come down. It's partly just the funding of inventory growth at Lugano.

[indiscernible] yes. So we expect really strong growth. So I would say because of both the cash flow, kind of generation power of the company as well as the growth and the expected deleveraging back down into our financial policy target range, which goes to kind of 3.5x at the high end, we still feel comfortable doing a deal. And yes, we could push leverage up into the 4s kind of temporarily here at the beginning of the year. But then we expect it to fall kind of back down below that.

Obviously, it's dependent on size of deals, it's dependent on multiple that we pay. And so it's a little hard to be precise until we have something kind of in our sight. I would tell you we will not take our leverage to 5x. And so that's off the table. But could it go over 4x to consummate a deal the size of The Honey Pot or a little bigger? Absolutely. And given the confidence that we have in our earnings trajectory right now and the cash flow producing power of this business, we are absolutely comfortable with that and the fact that our deleveraging post an acquisition will bring us back in line to where we need to be.

Lawrence Scott Solow
CJS Securities, Inc.

I appreciate that color. And then the second question, maybe a 2-part question. Just on the inventory headwinds of '23 and it feels like maybe those are certainly subsiding significantly, right? And you mentioned maybe it turns to a tailwind in '24. Can you just discuss sort of specifically BOA and PrimaLoft, I think, were the 2 bigger brands that were kind of impacted and sort of the underlying trends at both those businesses? Maybe a little more color there and the upside to guidance perhaps that you mentioned, would that be kind of maybe the inventory actually did turn into a tailwind?

Elias Joseph Sabo
Partner & CEO

Yes. So I'm going to let Pat speak specifically to some of the trends we're seeing at BOA and PrimaLoft and how that headwind, which we think sort of turned neutral in Q4. It was no -- were not a headwind nor a

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tailwind, how that will hopefully build into '24. But let me address the last part of that first, which is built into our guidance. We have not built a tailwind from inventory and sell-in matching sell-through, we have not embedded that into our guidance.

And that's why if there's one thing, I would say, to take from this call is it's just too early. We gave you 3 weeks ago a guidance range. It would be too early for us to increase that right now, and I think that would be irresponsible. However, if we were reissuing guidance today, we'd probably be more optimistic. And, I think, there are clear catalysts for kind of us to exceed the range here, and it could be material.

And one of those catalysts could be inventory changes starting to become a tailwind where sell-in just has to match sell-through. Forget the fact that there could be inventory building again at some point. We just want to get back to the point where inventories are no longer depleting which has been sort of a constant theme over '23. So there's absolutely upside that is available for that. I would tell you that we were a little bit shell-shocked by kind of the depth of the inventory changes of '23. And so we've been hesitant to build that in. But we think that's some nice upside that could exist as we go forward. And I'll ask Pat to comment on your questions on both PrimaLoft and BOA.

Patrick A. Maciariello
Partner & COO

Yes. So BOA is strengthening. And, hey Larry it is -- and it's tough to kind of tease out what part of that is model count, what part of that is an easing of pressure -- model count growth, what part of that is an easing of these headwinds that we talked about and what part of it is just really strong execution by the management team? Clearly, there's aspects of each, and I can't point you to kind of percentages.

But I can tell you that collectively, those are each having, each driving kind of bookings to be better than we saw on a year-ago basis, right? So at PrimaLoft, I'd say the language from customers is clearly that these headwinds are easing the language from customers is clearly that we're going to have a more stable, solid 2024. However, many of the brands are willing to chase the season, if you will, and not sort of order in advance. So there's just a little bit of a lag, but that's how I differentiate kind of those 2 if that makes sense. It feels like the easing of BOA is a little bit ahead of the easing of PrimaLoft.

Operator

Your next question comes from Matt Koranda of ROTH MKM.

Michael David Zabran
ROTH MKM Partners, LLC, Research Division

It's Mike Zabran on for Matt. Maybe just starting with the '24 guide. I [need to cut] the industrial segment adjusted EBITDA to get to the midpoint of $140 million. I guess, just based on recent underperformance relative to our expectations, I wanted to cut out of Sterno. But at the same time, we are facing 2 straight years of negative growth there.

So I guess just -- are we still expecting low to mid-single-digit growth in the industrial segment for '24? And maybe just give a bit more color on where we're seeing headwinds in the industrial segment and which, I guess, business we expect to be the heaviest drag in 2024?

Ryan J. Faulkingham
Executive VP, CFO & Co-Compliance Officer

Yes. So I'll let maybe Pat touch on kind of the industrial drivers, but I think you might be off on your numbers. So industrial for full year produced adjusted EBITDA of $128.6 million. So the midpoint of our guidance that we provided implies kind of a 1%, 2% growth as we think about 2024. I think we'd all agree that's a little bit conservative. As you mentioned, there's not a lot to cut here, right? Altor is performing well. Arnold is performing well. Same with Sterno. So I think we feel like there's upside to that midpoint. But Pat, do you want to provide any other kind of color on the industrial trends that you think will benefit 2024?

Patrick A. Maciariello

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Partner & COO

Yes. I just don't know about the underperformance at Sterno. I'm not seeing that. I mean, by our count and what we published, we grew sort of 11% to 12% there. And I don't see -- I guess I can't answer your question because I don't agree with the basis of your question, if that makes sense, respectfully.

Michael David Zabran
ROTH MKM Partners, LLC, Research Division

Yes. No. Sorry, just meant underperformance relative to our numbers that we had in our model, but totally understand where you're coming from. Maybe just anything stimulating growth in 2024 and kind of -- yes, just where we expect the growth in Industrial to come from in 2024?

Elias Joseph Sabo
Partner & CEO

Yes. So let me just give kind of a high level here. So we grew mid-teens on a consolidated basis in '23 over '22. That is far in excess of our core growth rate in industrials. And so I think we're all a little hesitant to get over our skis right now and say that you can back up an extraordinary year where you sort of triple your core growth rate and have not some payback that could happen from that.

A lot of that is due to margin expansion that occurred in '23 as a result of commodity price deflation. And as we've been saying, we've passed a lot of that commodity deflation to our customers, which is why revenues were down slightly, but EBITDA grew so rapidly. So our industrial businesses performed exceedingly well in '23, and they entered '24 with really healthy backlogs.

Now that said, I think we're a little cautious, which is why we only guided to sort of kind of 1%, 2% growth year. And that's -- it's not really based on what we're seeing in numbers manifest right now. It's much more based on the fact that we came off of a really extraordinary year. We don't know if that will get paid back some in 2024. But frankly, there's really no reason to expect that the company is not going to grow back at it or the industrial group isn't going to grow at its kind of normal longer-term rate of mid-single digit.

I would say, as Ryan mentioned, it is being conservative and we think that's just kind of prudent given the macro outlook right now. I mean remember, there are global tensions and wars that are happening kind of in Europe. And so you just have to be cognizant of kind of those threats that are out there, and we want to make sure that we are guiding appropriately. But I would say some upside exists to our guidance numbers. Specifically, Arnold is doing really well. Sterno, as Pat said, kind of grew double digits year-over-year. It's -- we have decent expectations for them to grow again. And Altor is performing really well, and we have an exceptional management team there.

So there's no real like issues that I could point to in any one of the companies other than to say, again, when you've tripled sort of your core growth rate in a year, you're a little hesitant to go too far out on your skis in the following year, but there is no reason we should underperform our core growth rate of mid-single digit this year.

Michael David Zabran
ROTH MKM Partners, LLC, Research Division

Got it. Makes sense. Switching to the consumer side, at 5.11, given we're pausing store growth strategy this year, maybe just speak to where we're planning to deploy that capital at 5.11 and just help us level set growth expectations for 2024?

Patrick A. Maciariello
Partner & COO

Sure. So first, kind of going backwards. We believe we will have another year of growth, probably similar to this year outside of what we alluded to earlier that there might be some charges for the [PPaaS] transition, right? So we think we will have a growth level that's consistent with prior year's growth in 2024, if that makes sense.

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As far as where we're reallocating, I mean we're trying to be best-in-class sort of in the DTC sector. So we're trying to get better at customer service. Everybody's always trying to get better at customer service. But we're really trying to provide best-in-class experience to our customers online as well and drive that online business, if that makes sense.

Secondarily, we're seeing -- we mentioned -- we've mentioned some of the geopolitical tensions that drives our professional growth as well. And we're seeing strong growth in professional and we believe we'll continue to see strong growth in professional.

Operator

Your next question comes from Kyle Joseph of Jefferies.

Kyle Joseph
Jefferies LLC, Research Division

Ryan, obviously, the portfolio has evolved over the past couple of years. But can you just kind of refresh it? I think you touched on this in your commentary, but on the seasonality in terms of adjusted earnings?

Ryan J. Faulkingham
Executive VP, CFO & Co-Compliance Officer

Yes. So seasonality adjusted earnings, it's -- I think if you look back at prior years, it's pretty representative. I mean, similar to what we said on cash flow is first quarter is generally -- first and second quarter kind of generally slightly weaker than the third and fourth quarter because a lot of our businesses have momentum to close out the year, whether it be the outdoor season or the holiday season, et cetera.

So no one business in particular, Lugano obviously is a pretty significant percentage of our business now. That business doesn't have a tremendous amount of seasonality given the fact that there's events or anniversaries or birthdays, et cetera, all year, but they do tend to have a little bit more in the fourth quarter around the holiday season. People generally, I guess, become gift giving around that. So outside of that, I'd say, again, kind of -- if I were modeling, I'd say roughly 60% back half, 40% front half is how I would think about it.

Kyle Joseph
Jefferies LLC, Research Division

Got it. Helpful. And then in terms of adjusted earnings guidance, I think you talked about a dollar per share basis being relatively flat year-over-year. The headwinds there are just a higher share count and the tax rate, I think you mentioned or anything else we should be thinking about? Because again its a new model for -- you guys did really strong EBITDA growth.

Ryan J. Faulkingham
Executive VP, CFO & Co-Compliance Officer

Yes. So Kyle, I mean last year, it's always tough to compare adjusted earnings when you have a discontinued operations, right? So last year, we pulled out ACI and Marucci, right? So that lowers our adjusted earnings. So the way I would think about it is we had guided on the third quarter earnings call, adjusted earnings between $130 million, $140 million, roughly. I think if we had owned Marucci the whole fourth quarter, we certainly would have beat that guidance, but we see this year being up slightly to 2023.

So I think there is growth in adjusted earnings. I think the challenge that we have with respect to adjusted earnings is Lugano because Lugano's growth carries with it less leverage of adjusted earnings because you've got -- it's a taxpayer, number one. And number two, it's got a pretty high noncontrolling interest shareholder, right? The management team owns north of 40% of the business. So that creates a pretty high level of noncontrolling interest that lowers adjusted earnings.

So we're going to have, as we've indicated, pretty substantial subsidiary adjusted EBITDA growth year-over-year, but not as high of adjusted earnings growth given that most of our growth would be Lugano.

Elias Joseph Sabo

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Partner & CEO

But Kyle just to point out, you could -- yes, just to point out the tax rate differential is a significant drag coming into 2024. We had roughly 7% of adjusted EBITDA, a subsidiary adjusted EBITDA, and we're modeling in 10% now. So if you take that 300 basis points on $500 million, it's $15 million, it's $0.20 a share. So if you were at [$2.23] versus [$2.03], and that's just having same tax rate the adjusted earnings growth per share or an adjusted earnings would be commensurate to the adjusted EBITDA growth.

And what Ryan has said is also true when Lugano carries higher growth, it comes with lower adjusted EPS growth because of the minority interest and capital investment. But I just want to be like very clear here that if the tax rate is to stay the same, we would expect to get some leverage on adjusted earnings and adjusted EPS from our adjusted subsidiary EBITDA.

Operator

Your next question comes from Mark Feldman of William Blair.

Mark Feldman
William Blair & Company L.L.C., Research Division

So just a question with some of the recent management changes, I know you had changes at 5.11 and PrimaLoft. Can you just talk to any major changes in strategies at both of those companies or priorities? With PrimaLoft, obviously, there's a lot of interest in expanding into newer verticals and new products. So just any update you can provide?

Patrick A. Maciariello
Partner & COO

Sure. I mean in PrimaLoft, it's a couple of things. It stayed the course, it's got a great business, a great IP. I think we probably would like to invest in branded PrimaLoft a little bit more and bring forth a little bit more of what PrimaLoft provides to the end user. And Anne Cavassa's experience there is very strong, and so we're excited to have her.

At 5.11, Troy Brown, who very high positions at Zumiez for many years, along with many other businesses like that -- in relevant businesses is really, we believe, a very strong operational excellence. And he will be working with Francisco Morales there as Francisco understands brand and product development, and will stay on as Executive Chairman. And Troy, we just believe is very strong in driving operational efficiencies and at delivering for the end customer in a DTC environment. And we think that combination will really yield tremendous benefits.

Mark Feldman
William Blair & Company L.L.C., Research Division

Got it. I appreciate that. And then I guess one other question as it relates to the consumer brands. You talked about 5.11 and BOA inventory destocking. But, I guess, one other subsidiary that would be impacted would be Velocity. So if you could just talk about trends there and anything else that you're foreseeing? And then any changes in strategies with that business going forward?

Patrick A. Maciariello
Partner & COO

Yes. It's a tough -- I mean it's -- it's 2 or 3 businesses. But -- in the archery side, we've seen some of that same destocking and -- or some inventory reduction levels that have hit the business. I'd say we're excited about the new products that we're coming out with this year in archery and we think it will be really -- they'll be well received later in the year by customers.

On the sort of more Crosman side, it just continues to have slightly weaker or weaker POS than we would hope, really driven by a lot of buying kind of during the pandemic era. And so a lack of replenishment really needed. So we're working every day to write the course there. But that's also one of the benefits of

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having a diversified business of 10 companies, right? And so -- but we continue to be focused and working every day there.

Operator

Your next question comes from Robert Dodd of Raymond James.

Robert James Dodd
Raymond James & Associates, Inc., Research Division

Almost back to Larry's question. On the leverage question, I mean, when would it be realistic for you to be entering the health care vertical? You said you'd be willing to take up leverage a little bit, but health care businesses do tend to go for pretty high multiples. So I mean [NextGen], which is probably a different scale than you're looking at, and we went for 30x EBITDA.

So with that dynamic, if the leverage did go up to the mid-4s, would you be then out of the acquisition market for maybe a couple of years to grow EBITDA to get the leverage down into your 3, 3.5 target range? Or what's the thought there on making acquisition now potentially reducing your ability to take incremental opportunities unless you make a sale, obviously, that's a different question.

Elias Joseph Sabo
Partner & CEO

Yes, Robert, I would say, one, we're not paying 30x EBITDA for our business. So that's off the table. I think that the businesses we're looking at, are trading at a premium to where the kind of innovative and disruptive consumers businesses are trading right now, call it -- if those are in the 12, 13, 14x range, good innovative health care businesses that have real good kind of moats around them are probably a 20% premium to that. Just to give kind of some type of kind of baseline.

So I think if we were to do a deal today in health care, it's going to bring us temporarily probably to kind of mid-4s maybe or depending on the size of the deal, again, it's -- we'd have to figure out how big the company is. If it's a $50 million EBITDA company, it's going to bring the leverage up more than if it's a $20 million or $30 million EBITDA company. And so a little bit of that is fluid. I will tell you that we have been, over the last few years, opportunistically divesting some businesses. That's not going to stop.

And so part of our commentary in our script is we are trying to move away from businesses that grow in line with our industry. And look, we own some great businesses that grow in line with their industry, and we still have some in our portfolio. And a lot of times, they're really niche businesses or niche kind of industries that they're in, they're market share leaders, probably create good cash flow. But we really moved to want to own companies more like BOA and PrimaLoft and Lugano and Marucci, which we had a huge kind of transaction in salon recently.

So those are the companies that we've been consciously moving towards. And at the same time, we've been making a concerted effort to sort of get rid of some of the companies that grow kind of with their industry. So I think there -- we will always be looking at making those portfolio changes. And as we kind of gear up and buy another business, whether it's in health care or consumer, there's probably going to be a couple more divestitures over the next 12 to 24 months that helps to bring leverage down and because the companies that were growing and are more core in our portfolio are growing at such a higher growth rate, we feel real conviction that our leverage comes down pretty dramatically just through free cash flow generation and through growth in the portfolio.

And so I get your concern and clearly that's something we're managing every day too, which is how much acquisition dry powder do we have, where do we want to deploy it, what are the best opportunities. And when we get to a leverage level that sort of gets to -- it's at a point where we're comfortable, but any more leverage would push us out of our comfort zone. Then it really kind of dictates that we look at raising capital, selling some of the companies to continue the portfolio repositioning, those things are on the table.

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And look, historically, we've raised capital opportunistically in kind of interesting ways. The ATM has been used historically when the stock price reflects closer to fair value. We don't feel that's the case right now. We've issued preferreds, which are nondilutive. And so there are other components of capital that we think can become available to us that don't necessarily dilute shareholder equity to the extent we have a great opportunity. Now ultimately, we're always balancing, what is the cost of that capital versus what is the new opportunity that we're bringing in.

And if we can drive a significant enough discount on the upfront purchase price, we're willing to pay a little bit more for our capital. And so it's a balancing act right now. I can tell you that we feel firmly in the market for both health care and consumer businesses. We are comfortable taking our leverage up a little bit. But it's hard for me to say, does the next deal then prevent us from being back in the acquisition market because I don't know what our leverage profile is going to look like upon that next deal. And you all wouldn't be privy to what we're currently working on that may be divestitures too until we get kind of those closed.

But this portfolio transformation that has been kind of a big undertaking of the entire management team, since I took over in 2018, is not going to stop until we get sort of the portfolio that we are looking for, which is as I said, and you're going to hear these words a lot. We're looking for great innovative, disruptive businesses. And at some point, what we will own in our portfolio, we were not going to be owning companies that are more growing in line with our industries. That was sort of a legacy business model and we will transition this portfolio over from -- so what we had in legacy to sort of the new vision and that's going to free up capital to continue to deploy.

I think the other thing to keep in mind is that these businesses are generating faster levels of growth. And so our full expectation is, as we continue to execute on this, our growth rate is going to continue to pick up our core growth rate. And one should be more comfortable with a slightly higher level of leverage, when you have better quality businesses with more defensibility around those companies, they have better growth profiles longer term because they're able to take market share, not just grow in line with their industries.

Robert James Dodd
Raymond James & Associates, Inc., Research Division

Very helpful, I appreciate all the color. Now, flipping the other way, if I can, companies have been almost "too successful." I mean Lugano, I mean, look -- back of the envelope for me, it looks like it could be as much as 1/3 of consolidated subsidiary EBITDA next year because it's been so successful. At what point does it get too big? Like, it's very successful, it's not growing in line with its industry. It's massively outgrowing that. But at what point does it become too much? Or is there just no line which is too much of a share of subsidiary EBITDA then it becomes a concern for you that you don't have the countercyclicality if it's dominating everything and you would join the company?

Elias Joseph Sabo
Partner & CEO

Yes. It's a great question, Robert. I mean Clearly, the D in CODI, and we keep talking about the benefits of diversification start to slow down, and we don't really have those benefits. To the extent that one of our companies starts representing too large of a component of our overall earnings.

So like -- it's a valid question.

And Lugano's growth rate and sort of what Moti and Idit have built there. it is just truly phenomenal. It's honestly one of the businesses that I've just never seen anything like it. I don't think there's many businesses that are as good as this company that are out there. And so on the one hand, you kind of don't want to let go. I think kind of rule #1 in portfolio management theory, and we're not stock traders. So this doesn't really apply. But you kind of rise if you're winners and you get out if you're a loser.

It's -- kind of that rule applies here a little bit. This is a business that, look, it's still got -- it's kind of massive TAM. It's got huge market potential and opportunity. It's got a visionary founder and leadership team, and we have the capital to support its growth needs. So that argues for holding it and continue to

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let that growth benefit our shareholders. On the other hand, there is a point where it becomes too big, and it sort of overwhelms the system. And so that's something that we're on the lookout for.

I think if it becomes 1/3 of our EBITDA, like you referenced, we're going to have a really good year this year because you're talking about a business that's going to generate kind of growth rates similar to 2023. And I promise you that is not built into our guidance at all. I think if we're getting there, it probably is something where if we're looking at the end of '24 and saying this company represents 1/3 of EBITDA, and it's still growing at double the growth rate or triple the growth rate of our overall company then we're probably considering different options for financing the business. And I think there are a plethora of opportunities where we could continue to kind of participate in the growth and -- but not have it be all funded by us.

So that will be explored sort of depending on how '24 develops. But this is a really high-class problem for us to have. And your point is a good one. And I would tell you this isn't -- this is not a company that we look at and say, we want this to represent 50% of our EBITDA. So if it continues to grow at historical growth rates, it's going to be a really great '24, and we're going to evaluate kind of what that means going forward and how we would want to think about financing in that context of the business as it goes forward.

Robert James Dodd
Raymond James & Associates, Inc., Research Division

And yes, it's just a tremendous success. So it is a high tax problem.

Elias Joseph Sabo
Partner & CEO

Thank you, operator. As always, I'd like to thank everyone again for joining us on today's call and for your continued interest in CODI. Thank you for your support.

Operator
Thank you. This concludes Compass Diversified's conference call. Thank you, and have a great day. You may now disconnect.

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