S&P Global
Market Intelligence

Compass Diversified NYSE:CODI

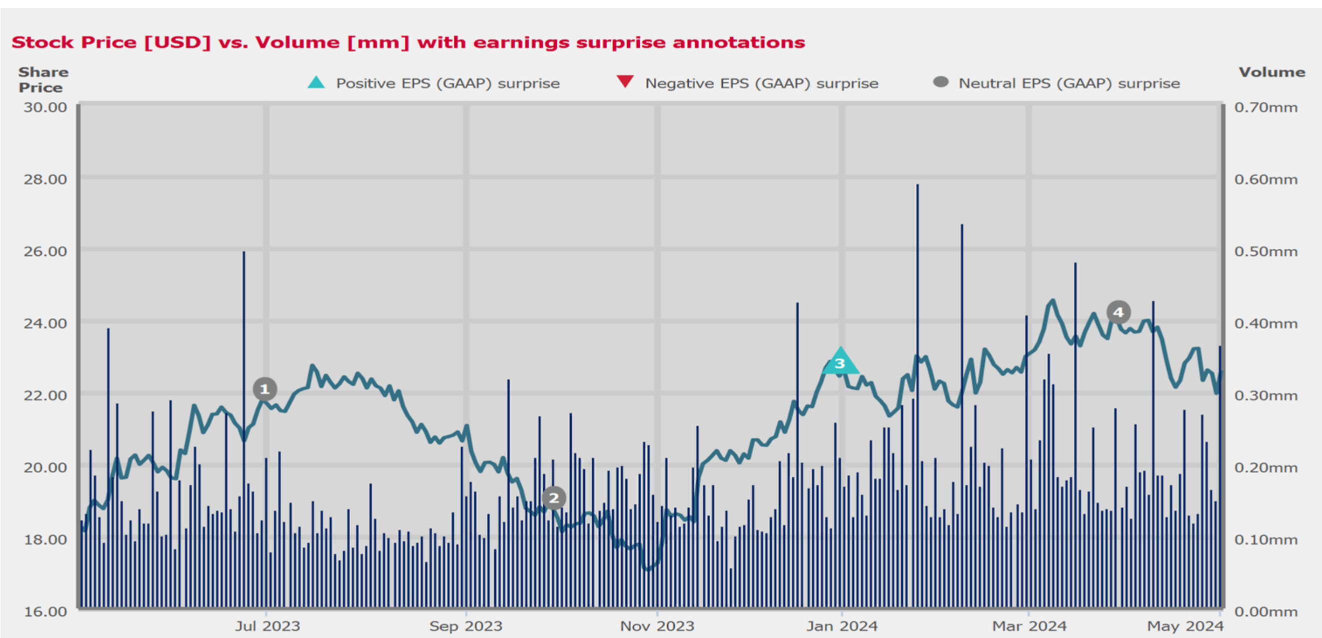
FQ1 2024 Earnings Call Transcripts

Wednesday, May 01, 2024 9:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2024-			-FQ2 2024-	-FY 2024-	-FY 2025-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS (GAAP)	0.17	(0.02)	NM	0.15	0.72	0.95
Revenue (mm)	541.88	524.29	▼(3.25 %)	554.39	2321.21	2482.89

Currency: USD
Consensus as of Apr-17-2024 1:42 PM GMT



- EPS (GAAP) -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2023	0.19	0.19	1 0.00 %
FQ3 2023	0.20	(0.33)	NM
FQ4 2023	0.03	1.70	▲2 5566.67 %
FQ1 2024	0.17	(0.02)	NM

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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

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Derek Sommers
Jefferies LLC, Research Division

Lawrence Scott Solow
CJS Securities, Inc.

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

Matthew Butler Koranda
ROTH MKM Partners, LLC, Research Division

Matthew Philip Howlett
B. Riley Securities, Inc., Research Division

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

ATTENDEES

Cody Slach
Gateway Group, Inc.

Presentation

Operator

Good afternoon, and welcome to Compass Diversified First Quarter 2024 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 First Quarter 2024 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 Q1 2024 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-Q 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 and 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 changing 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 yet another strong quarter of results. We once again exceeded our expectations. Our success in this first quarter can be attributed to our deliberate focus on owning and managing a growing number of innovative and disruptive businesses that have industry-leading growth potential. This strategy not only reduces financial volatility, but also accelerate our annual core growth rate.

As we saw this past quarter, the diversification of our subsidiaries mean that if a few of our companies lag in growth, others may be able to compensate, resulting in a more consistent and reliable growth engine. This quarter, we saw the strongest performance from our branded consumer vertical, which reported 11% growth in pro forma revenue and 22% growth in pro forma adjusted EBITDA. Pat and Ryan will, of course, go into greater detail, but I will tell you, Lugano produced another quarter of remarkable results, and the company currently shows no signs of slowing down. With the opening of its new London salon earlier this week, we believe international expansion will be a huge opportunity for this business.

You will remember, we were expecting both BOA and PrimaLoft to rebound against the inventory destocking headwinds of the recent past, and we believe they are now through the worst of it. I am pleased to announce BOA had a great first quarter, better than expected. While PrimaLoft continued to see revenue and adjusted EBITDA declines in Q1, they saw bookings growth in the first quarter, which provides confidence they will return to growth in the second quarter.

The Honey Pot Company, a business we only acquired in the first quarter of this year, is already integrated with a newly appointed world-class Board of Directors, and we are seeing significant gains in shelf space across key retail partners. Additionally, point-of-sale data remains robust, reflecting strong consumer demand for The Honey Pot Company's better-for-you products.

Thanks to the strong performances that Lugano, BOA and the acquisition of The Honey Pot Company, adjusted earnings for this quarter were above our expectations and up significantly over Q1 of last year.

I'd also like to briefly discuss the divestiture of Crosman, the air gun division of Velocity Outdoor to Daisy outdoor products. We are grateful for its contributions to Velocity Outdoor and CODI, and I want to thank the entire Crosman team for their dedication over the years. Velocity Outdoor continues to be a subsidiary, specializing in archery and hunting apparel, and we are excited by its planned product launches in the coming years. This opportunistic divestiture of Crosman also aligns with our strategic focus of adding value through the management of innovative and disruptive companies that are poised to outpace industry growth rates. We believe Crosman's sale to Daisy, a recognized industry veteran in the air gun space, positions it well for future success.

Despite our outperformance in the quarter, continued elevated inflation, delayed rate cuts and heightened geopolitical risks, all combined to create a weakening macroeconomic backdrop, which has negatively affected our industrial vertical. Across our 3 industrial businesses, we saw a slight decline in both revenues and adjusted EBITDA in Q1. However, we remain confident in the positioning of these businesses and anticipate our industrial vertical could possibly see modest growth later this year.

All in all, I am extremely pleased with our first quarter. This is our strategic repositioning in action.

Despite a mixed economic environment, we delivered a strong first quarter. Both our results for the quarter and our outlook for the rest of the year demonstrate that owning and managing a diversified group of companies with a growing share of disruptive, high-growth businesses is the right strategy and we believe positions our business for sustained outperformance.

We believe across our branded consumer vertical, inventories are now more balanced, and we expect the headwinds suffered in 2023 to turn into tailwinds for the remainder of the year. We also believe through company-led innovation, our industrial vertical could see another year of modest growth in 2024 and is positioned well for 2025.

Combining our first quarter performance with our forward momentum, we are feeling bullish about the rest of the year, so we are raising our full year adjusted earnings outlook, which Ryan will detail for you in just a few minutes.

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 The Honey Pot Company as of January 1, 2023.

I'm pleased to report on another successful quarter. On a combined basis, revenue and pro forma adjusted EBITDA grew by 4% and 15%, respectively, in the quarter. Though Lugano once again was a significant driver of our growth, growing revenue and EBITDA by 61% and 83%, respectively, we continue to see positive trends throughout our business. Within our industrial vertical, for the first quarter of 2024, revenues decreased by 10% and adjusted EBITDA decreased by 3% versus Q1 2023.

Arnold continued to grow revenue in the quarter though experienced higher SG&A costs due to increased sales and marketing expenses and the timing of certain professional services fees. Bookings for the quarter significantly outpaced revenues, and we believe the company remains poised for a solid 2024 and continues to build upon its long-term project pipeline.

At Altor, revenue declined slightly as we experienced churn in projects with a couple of our larger customers. The pipeline of new products is robust, however, and we believe the company will return to revenue growth in the back half of this year. We also note that Altor continues to increase margins in the face of revenue headwinds, and we remain confident in the business and the team.

Sterno grew adjusted EBITDA slightly in the quarter as the strength of the company's foodservice division offset slightly weaker demand levels in its scented wax division.

Turning to our branded consumer vertical. For the first quarter of 2024, pro forma revenues increased by 11% and pro forma adjusted EBITDA increased by 22% versus Q1 2023. As Elias mentioned, clearly, the strongest performer in the quarter remains Lugano. We saw growth in each salon and geography and benefited significantly from investments made in our flagship salons in Newport Beach and Palm Beach. This week, the company opened its long-awaited London salon. And though early, by all accounts, the opening has been a success, and we look forward to expanding the Lugano model internationally.

Last quarter, we touched specifically on 2 of our businesses furthest up the supply chain, BOA and PrimaLoft, and how order patterns were normalizing as their respective channels cleared. At that point, it appeared that BOA was perhaps a bit more than a quarter ahead of PrimaLoft in clearing the inventory headwinds in their supply chains and returning to growth.

We are pleased to report that BOA grew revenues and adjusted EBITDA by 13% and 15%, respectively, in the first quarter of 2024. In addition, bookings outpaced revenue growth, which supports our expectations of a strong 2024. At PrimaLoft, though revenue and adjusted EBITDA continued to decline in Q1 of 2024, we did see solid double-digit bookings growth in the quarter, which gives us increased confidence as we enter the second quarter.

Touching on our newest business, The Honey Pot Company. It performed in line with expectations as revenues were approximately flat and adjusted EBITDA declined slightly in the first quarter of 2024 on a pro forma basis. Consistent with our understanding at the time of the transaction, the company had one large promotional event at retail in February of 2023 that did not repeat in the same magnitude this quarter.

In addition, the company continued to add infrastructure, including head count and a dedicated distribution center to support its growth, which pressured adjusted EBITDA margin slightly. Importantly, though, the company grew point of sales for its core products in almost all its retail partners and added shelf space for new products with several partners so far this year. We remain excited about The Honey Pot Company and expect a solid year in 2024.

5.11 was approximately flat in revenue and up slightly in adjusted EBITDA in the first quarter of 2024. Strong revenue growth in the professional channel offset both market-related and self-induced challenges in our DTC channels. We've seen improvement in these areas subsequent to quarter end, and we believe the 5.11 management team is taking the right actions, and the company is on solid footing.

As a whole, we were very pleased with the first quarter and have confidence in our increased outlook for the full year.

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 March 31, 2024. I will limit my comments largely to the overall results for CODI since the individual subsidiary results are detailed in our Form 10-Q that was filed with the SEC earlier today.

On a consolidated basis, revenue for the quarter ended March 31, 2024, was $524.3 million, up 8% compared to $483.9 million for the prior year period. This increase was primarily a result of The Honey Pot Company and strong growth at Lugano and BOA, which was partially offset by lower revenue at Sterno, Altor and Velocity.

Consolidated net income for the first quarter of 2024 was $5.8 million compared to net income of $109.6 million in the prior year. The first quarter of 2024 included an $8 million goodwill impairment charge at our Velocity Outdoor subsidiary. Net income in 2023 included a $98 million gain on the sale of Advanced Circuits.

Adjusted EBITDA in the first quarter was $94.8 million, up 28% compared to $74.1 million in the prior year. The increase was due to the acquisition of The Honey Pot Company and strong growth at Lugano and BOA. Included in adjusted EBITDA in the first quarter of 2024 and 2023 were management fees and corporate costs of $21.4 million and $19.4 million, respectively.

Adjusted earnings for the first quarter were above our expectations, coming in at $34.3 million. This is up significantly from $19.8 million in the prior year quarter due to strong performances at Lugano and BOA.

So now moving to our 2024 guidance. As a result of the strong performance in the first quarter and our expectations for the remainder of the year, we are raising our subsidiary adjusted EBITDA guidance by $10 million. However, with the sale of Crosman, we are reducing our guidance by a similar amount. Thus, our full year 2024 subsidiary adjusted EBITDA is consistent with what we provided on our last earnings call of between $480 million and $520 million despite the sale of Crosman.

The subsidiary adjusted EBITDA range for our industrial vertical remains $125 million to $135 million. The subsidiary adjusted EBITDA range for our branded consumer vertical remains $355 million and $385 million. We expect full year 2024 adjusted EBITDA to be between $390 million and $430 million. This range factors in an expected $86 million in corporate-level overhead and management fees in 2024. This compares to $341 million in adjusted EBITDA in 2023.

Now on to adjusted earnings. With the paydown of revolver debt outstanding of approximately $60 million, which includes proceeds from the sale of Crosman, we are increasing our full year 2024 adjusted earnings guidance range by $3 million and expect it to be between $148 million and $163 million. At the midpoint of this range and assuming the same share count at March 31, 2024, of 75.3 million shares, we expect to earn $2.07 in adjusted earnings per common share in 2024.

A note for investors and analysts, the Crosman sale will not be recorded as discontinued operations, and thus, we expect we will record a relatively small financial statement impact from the sale in the second quarter, we plan to offset any positive or negative impact from the sale in our adjusted earnings calculation in the second quarter and for the full year of 2024.

Turning to our balance sheet. As of March 31, 2024, we had approximately $64.7 million in cash, approximately $552 million available on our revolver, and our total leverage ratio was 3.84x. Our leverage at the end of the quarter was lower than we anticipated as a result of strong operating performance. We used our proceeds from the sale of Crosman to pay down revolver debt outstanding, and thus, absent any acquisitions in Q2, we expect our total leverage ratio to decline in the second quarter.

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 first quarter of 2024, we used $13 million of cash flow from operations. Lugano used $65 million in cash flow from operations to support its continued extraordinary growth. Outside of Lugano, our subsidiaries produced $52 million in cash flow from operations in the first quarter, allowing us to reduce our leverage, as stated earlier.

And finally, turning to capital expenditures. During the first quarter of 2024, we incurred $7.7 million of CapEx at our existing subsidiaries compared to $14.9 million in the prior year period. The decrease was primarily a result of a decline in 5.11 store rollouts in 2024.

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 will now turn the call back over to Elias.

Elias Joseph Sabo
Partner & CEO

Thank you, Ryan. I would like to close by recognizing a significant ESG milestone and also by giving you a brief update on our view of the current M&A market.

On the ESG front, I am proud to announce that earlier this week, we released our inaugural sustainability report. The report provides insight into how we manage ESG both at CODI and at our subsidiaries. It outlines our ESG framework and the actions we have taken, designed to bring about social and environmental benefits. This report underscores our belief that ESG is an ongoing commitment, and we are dedicated to achieving substantial deliberate progress. You can view the report on our website to learn more about our vision and our progress to date.

We have made significant strides over the last few years, and this progress wouldn't have been possible without the engagement of our Board, our leadership team and, most importantly, the participation of our employees, both at CODI and at our subsidiaries. Our goal remains to make improvements that align with our company values and create strong financial returns for our stakeholders.

I would like to thank our Head of ESG, Zoe Koskinas, and her team for their passion and all the work they have put in to get us to this point.

When it comes to the M&A market, we feel a level of optimism that we have not felt in years. We continue to see an improvement in the quality of businesses coming to market. We also see our competitors continue to struggle with leverage buyout financing, specifically when it comes to branded consumer businesses. This only creates more opportunities for us.

When debt markets are weak for single asset buyouts, our competitive advantage grows. We believe today's market landscape allows our competitive advantage to shine, setting the stage for consummating M&A at more attractive valuations, which, of course, leads to improved shareholder returns.

We remain steadfast in our efforts to identify, acquire and manage disruptive and innovative companies. And as Ryan mentioned, our strong liquidity position enables us to act on acquisition opportunities and also invest in our subsidiaries to further build upon our track record of delivering growth for our shareholders.

While I have tremendous confidence in our strategy and our competitive advantages, I'd also like to take a minute to recognize our employees who deliver these outstanding results day in and day out. Thank you to our subsidiary management teams and employees and to the entire CODI team for your hard work executing this growth strategy.
With that, operator, please open the lines for Q&A.

Question and Answer

Operator

[Operator Instructions] And our first question comes from Larry Solow from CJS Securities.

Lawrence Scott Solow
CJS Securities, Inc.

Great. I guess first question, just -- Elias, just sort of following up on your -- I appreciate the commentary on the M&A market, and it sounds like you sound very enthusiastic there. So I'm just curious, would your leverage still relatively sort of at the higher end, I think, of the range you'd like it to be at? What's your appetite at these levels? And maybe the sale of Crosman, maybe are there other things in the wings that you might be able to do also to improve that leverage lower so you can be maybe even more aggressive? It sounds like opportunities [indiscernible].

Elias Joseph Sabo
Partner & CEO

Yes. So Larry -- yes, sure. So -- and I think we mentioned this on the last call, there is the ability to consummate acquisitions, and we're comfortable bringing our leverage up higher than where it is today. The reason we're comfortable is, frankly, what we've demonstrated here in the first quarter and in the fourth quarter and what we expect is going to continue, not only this year, but well into '25 and beyond. We've repositioned the company to just have a dramatically faster growth rate. And our ability to create cash flow and deleverage is really strong now.

And so I think the company profile allows it to handle more leverage temporarily because the earnings growth profile is so strong and our cash flow profile. Remember, Lugano used $65 million of cash, but it delivered 83% growth in EBITDA. Outside of that, our business delivered north of $50 million free cash flow from operations. And I do think you have to separate Lugano out given the extraordinary growth rate and the returns on invested capital there.

So we look at kind of how the company is positioned today. And with, as you mentioned, the sale of Crosman, which the proceeds of which will go to delever even further, we feel that we have a very strong deleveraging trend that's coming not only in the second quarter but beyond. And as a result of that, it's going to open up more capacity.

Now to the other part of your question, we have been -- since 2018 when I took over and Pat became COO, we've been kind of moving the portfolio around and creating much higher percentage of businesses that are more disruptive and innovative and can materially outgrow their core growth rate. The sale of Crosman is an extension of that, but that isn't done yet. And so I would say there are other assets in the portfolio, which are not growing at the level, or expected to, that we will continue to make some divestitures. And so we feel that there's adequate sources of capital that will be coming in, both through continued portfolio repositioning as well as growth in the portfolio, free cash flow generation, and then lastly, kind of when we can find opportunities to run the common and preferred ATMs.

Lawrence Scott Solow
CJS Securities, Inc.

Fair enough, and I appreciate all that color. And just the second point just on sort of the outlook. It sounds like maybe the macro -- I think, obviously, interest rates are staying up longer than, I guess, some had hoped. So maybe from a macro level, things are slightly worse for you guys, but it sounds like you have some specific offshoots at a bunch of your companies that are basically offsetting that all in. And then you have Lugano, which is still kicking it -- kicking a** there, and that's why the guidance is going off. Is that kind of a good way to sort of summarize the outlook in a broad-brush?

Elias Joseph Sabo
Partner & CEO

Yes. I mean we all thought Q1 GDP came in kind of disappointing, with inflation increasing a little bit. So I think that was kind of -- needs to be taken into consideration. And frankly, we're seeing it a little bit. In our industrial businesses, there is a little bit of weakness, but over 70% of our EBITDA comes from consumer. And we aren't seeing that same weakness there, Larry. I mean the consumer remains very strong and resilient.

Now clearly, depending where the consumer is, the more inflation has impacted a consumer, that spending pattern is a little lower. But remember, we skew towards the upper end consumer globally for the vast majority of our portfolio. And then we do have things that were massive headwinds last year like these inventory destocking at all of our consumer businesses and caused sell-in to be far below sell-through, that headwind is dissipating. So there's a factor that's sort of unique to our kind of group of subsidiaries right now that give us confidence that we're more likely to be surprising going forward on the upside than we are the other way.

Operator

And our next question comes from Mark Feldman from William Blair.

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

I guess on my first one, can you talk about any initiatives that you had at Velocity to -- also, you guys came off of a demand surge during COVID. And you are -- obviously saw the inventory destocking trends that you saw at PrimaLoft and BOA as well. So can you talk about any initiatives to work through that going forward now that we -- you sold off the Crosman division?

Patrick A. Maciariello
Partner & COO

Sure. Initiative, yes, I mean I would say, in short, it's a focus on technology and new product development. I think if you look at the archery side, we have some exciting new technologies coming out that we think could help accelerate sales in '25. And then if you look, the company's subsidiary, [Kings], is just a really on-trend hunting apparel business that each year continues to take market share, granted from a small base. So we're excited about both of those businesses.

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

Great. And then another one also on destocking here. So it's great to hear with the double-digit growth of bookings with PrimaLoft, but can you just talk about timing of when we can actually see those convert to revenue? I know there's seasonality built in with ordering, and when those have to be done by to see it in the actual results for the year?

Patrick A. Maciariello
Partner & COO

So we believe we'll grow in the second quarter at PrimaLoft. We believe we'll grow top line, and we believe we'll grow EBITDA. The quarter's bookings are not fully in yet, but I would just say all signs are pointing to growth as soon as this quarter.

Operator

And our next question comes from Derek Sommers from Jefferies.

Derek Sommers
Jefferies LLC, Research Division

Just on the industrial segment on the revenue decline, is that more of a price story or a unit or quantity story? And then kind of EBITDA margins held up a little bit better there. What's happening on the expense side of the P&L to have those hold up a little bit better?

Patrick A. Maciariello
Partner & COO

Yes. So I'd say on the revenue versus quantity, it is a little bit of both. On the Sterno side, we did see some pressure in our wax-melt business, which is predominantly sort of the middle income and below purchaser.

And then I think your second question, as it relates to margins and margin improvement, we're -- our management teams are doing a good job. We mentioned before and we've touched on the new management team at Altor, which continues to drive efficiency gains. We have a strong management team now at Sterno, and as well as we have at Arnold, they just had some -- got caught with the timing of some expenses this quarter, as I mentioned, on some professional services and marketing expenses.

Derek Sommers
Jefferies LLC, Research Division

Got it. And then just to pivot to Lugano on the London store rollout, kind of what's the -- do you guys expect like a 12-month runway to get this fully kind of operational and a good spot? Or kind of what's the time line for implementation, so to speak, there?

Patrick A. Maciariello
Partner & COO

I mean I think our stores -- our salons usually take some time to get up to sort of become optimized. I would say it is going to have sales and be a driver of sales, though, as soon as this week. It's a good store that we have a lot of expectations on. It's right there on -- right there in Mayfair. It's in a great location. It's beautiful. They're doing a lot of promotion around it. So we're confident it's going to have a positive impact on revenue almost immediately.

Operator

And our next question comes from Matt Koranda from ROTH MKM.

Matthew Butler Koranda
ROTH MKM Partners, LLC, Research Division

I guess on the Crosman portfolio action, I'm curious why only carve out Crosman, why not just sort of divest of the entire Velocity segment? Are we waiting for some improvement at Ravin and the other subsidiaries there?

And I just wanted to understand just on sort of your posture toward acquisitions going forward. It sounds a lot like we'd be comfortable making acquisitions first and then selling down certain assets to drop leverage, not necessarily -- we don't necessarily need to wait for divestitures as a gating item to get to the acquisitive stuff. So maybe just put a finer point on that for us, if you could as well.

Elias Joseph Sabo
Partner & CEO

Yes, Matt. So with Velocity, I would say the air gun business was performing okay, and we just felt that it made sense, and there was a natural buyer out there. We're combining the businesses, both which the industry has created some excess capacity. Over the last few years of declines, it kind of makes sense that those businesses would be combined. And I think Daisy have a great asset, and we'll be able to create a lot of efficiencies out of putting those businesses together. And so I think there's more value to be created by separating the 2 businesses and having the air gun business kind of be sold off first.

In terms of what is left and why not having sold the whole thing, we think what remains, as Pat said, has some really exciting new technology that's coming next year and has the potential to really reinvigorate the category and provide some substantial upside growth in kind of '25 and '26. And so I think it makes more sense given that's kind of consistent with what we like in our businesses, kind of highly innovative businesses that can drive kind of category growth. And we're going to -- we expect to see that here in Velocity next year.

So I think there's a better path to maximizing value out of the overall Velocity asset by having split the business up and kind of doing it as we are right now. And I think it's very much consistent with our strategy. And frankly, I think it is consistent along what our ESG strategy is as well to move on from that asset.

With respect to your second question in leverage, the answer simply is yes. We're comfortable taking on leverage now more than we have to fund an acquisition. And there could be the deleveraging activities that will happen after that, anywhere from selling under the ATMs to potential further divestitures, those are all there. And so the timing doesn't need to be fund on the ATMs or divest an asset in order to acquire. If we find a great $0.5 billion acquisition opportunity, we're going to execute against it. And we feel very comfortable with where our leverage is now, especially pro forma for the sale of the Crosman business and repayment of those proceeds towards debt reduction. And so we're very comfortable now going out and doing an acquisition.

And again, Matt, given the strength of the business, given the kind of growth in earnings that we are really confident about, especially in Q2, but really more so for the rest of the year and how it looks into '25, we're just comfortable having a little bit more leverage right now. And so the timing of kind of the portfolio repositioning is a little bit less relevant. No, we're not going to go haywire and go outside of kind of reasonable parameters, but bringing our leverage up another half a turn or 3/4 of a turn for a temporary period would not distress us given all the signs we're seeing of growth and deleveraging in our business.

Matthew Butler Koranda
ROTH MKM Partners, LLC, Research Division

Okay. Super clear and appreciate all that detail, Elias. I guess on the Lugano front, obviously, it was not an issue this quarter to lap some pretty big 2-year sort of stack comps there. But just wondering, as we progress through this year, why the confidence level is so high that we sort of continue to see the large growth rate that Lugano has been on for the last several quarters? Maybe just unpacking the drivers of that growth a little bit more clearly for us would be helpful, like how much is related to kind of salon expansion and some of the international expansion that you're alluding to versus just kind of like-for-like growth at existing salons and maybe AOV growth? It'd just be helpful to hear a little bit more on that.

Patrick A. Maciariello
Partner & COO

Yes. Matt, that's a lot to unpack. Let me take a shot at it. So first and foremost, I think the market penetration is incredibly low at Lugano. Particularly, we think we're converting non-jewelry buyers to jewelry buyers as well. So the market penetration when you include that is even lower, right, number one.

Number two, we're investing significantly in inventory as you can see and as we told you. And we're more and more getting the right pieces in the right places at the right time to be sold.

Number three, I think you will still see some maturation of some of the stores that we invested in, in the last couple of years, be that DC, particularly the Palm Beach flagship salon, particularly Newport Beach. I think you'll still see continued growth there as those stores -- salons, excuse me, just continue to mature.

And then I'd say, lastly, there will be geographic growth. Obviously, having a London salon now open will drive growth. There are a couple more areas or cities we're looking in, though I wouldn't expect any announcements probably until the fourth quarter at the earliest. So I think it's a combination of all of the things you said, plus investing in the right products.

And I'll just remind you, this is a disruptive business that's able to convey a lot of value to their customers through their disruptive supply chain as well, right? We believe we're able to buy very well and pass on that value to the end customer.

Matthew Butler Koranda
ROTH MKM Partners, LLC, Research Division

Okay. Super. Can I sneak one more in just on Honey Pot since it's kind of newer? Just curious the growth drivers that you're seeing there. I think you guys alluded to kind of additional shelf space with some key retailers. Maybe just a little bit more on where you're seeing those shelf space gains, maybe in which product categories and which types of retailers you're seeing some gains there and just sort of the growth runway you see there.

Patrick A. Maciariello
Partner & COO

Sure. So there's a couple of big-box retailers that sort of dominate the industry. We are strong with both of them, particularly one getting stronger. Outside of that, it's really growth in drug and grocery channels, which we've been under-indexed to historically. And then there are some new products -- projects hitting the shelf now. We're very excited about sort of the new product pipeline in '25 and '26 as well.

Operator

And our next question comes from Robert Dodd from Raymond James.

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

Congratulations for the quarter. On PrimaLoft, I'm kind of [indiscernible] you said about the bookings, et cetera. And I know it's difficult to get see-through to the end consumer, obviously, inventory channel and the like, but do you know the source of -- is it the same products that are finally ramping back up or is this new SKU wins or new client relationships? Or any color on what's driving the turnaround? Is it just inventory clearing out or are there other factors at play with this one here?

Patrick A. Maciariello
Partner & COO

No, we're adding to some products. A couple of products have rolled off, but we're also adding, particularly in the performance segment, some new customers and some new project wins as well. And then I would say as far as -- it's also -- it's just what we're hearing as far as later order patterns, et cetera, it's just what we're hearing from our brand partners. And so I can't point to data specifically to that. But in general, they're saying that the supply chain is improving.

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

Got it. And almost same kind of question with BOA, right? Very strong quarter this quarter. It's been one that -- its mix has been historically a lot of snow boots and seasonality and snowboarding shoes -- boots, but you've been adding a lot of SKUs, you've been adding or trying to add new product verticals. I mean how much is the new responsible for this rebound versus -- I don't want to call it old because, I mean, the products aren't that old, but the older verticals versus newer verticals and SKUs driving it, how much -- what's the contribution there?

Patrick A. Maciariello
Partner & COO

Boy, that's a tough one to unpack. And I actually have some data on this to say that it's roughly half-and-half, it feels. We are growing our number of SKUs, but we're growing revenue at a faster rate than that. And so I think our SKUs are also taking market share.

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

Got it. And then last one, if I can, on Lugano. I mean, obviously, London is open now. Are you willing to articulate more -- are there international locations that have been scouted in process or is it still -- are you just not willing to name names in terms of countries and cities?

Patrick A. Maciariello
Partner & COO

Not willing to name names, but [been scouted and] not yet in process. Currently being -- yes.

Operator

And our next question comes from Matt Howlett from B. Riley Securities.

Matthew Philip Howlett
B. Riley Securities, Inc., Research Division

Just on the guidance, this inventory destocking, this headwind that's going to turn into a tailwind, the guidance has not incorporated the snapback that we've all discussed over the last few quarters that there could be a reacceleration at some point if this is really the end of it.

Elias Joseph Sabo
Partner & CEO

That is correct, Matt. The guidance assumes sort of the same trajectory we're seeing right now in the first quarter, sort of the slow turning of the boat, if you will. And it kind of is improving, and it feels like it's steadily improving, but it doesn't assume sort of a big snapback and rebound. And what we're hearing is that customers globally, after having so much excess inventory, are now just being extra cautious. And so -- and obviously, the cost of carrying inventory is a lot higher now where rates are. So I think that has a dampening effect on it.

But my sense is just given what we know like if you look at BOA, for example, and where we're getting more than 10% annual SKU growth over the last few years, you can start to run the math and say, okay, there should be a bigger rebound here, and we probably haven't cleared all the inventory yet and had -- kind of had stabilization.

So remember, these companies serve a lot of different end markets. They're not synchronized by any means. And so maybe rather than a snapback, it's a slow constant build that happened from the beginning of this year into next year, and it surprises by just continuing to build. But I would say this does -- our forecast doesn't reflect that inventories have sort of that snapback in or any continued progressive increases, although it's likely that, that probably will happen, which is why I say I think we're poised to surprise on the upside, not the other way around as the year unfolds.

Matthew Philip Howlett
B. Riley Securities, Inc., Research Division

Right. And just take BOA, for example. I mean normalized organic growth could be still something like 20-plus percent easily, right, when things get back to normalization. Just talking out loud.

Elias Joseph Sabo
Partner & CEO

Yes. I mean I think it's historically until we have some real craziness in the supply chain where we have massive over ordering, which benefited their numbers in late '21 and early '22, and then destocking. So if you kind of clear all that noise, BOA has been sort of a 20% plus or minus top line grower over kind of its history.

Now we don't sign up and say that's what we think the company is going to deliver, but it still has a lot of the same core attributes of relatively low market share, outstanding management, outstanding technology, great strategy and execution. And so it still has all the elements in place. But we don't like to get out over our skis, so we're not going to say that's kind of what we think its core growth rate is. We'll be a little bit more modest than that. But look, those things still exist, and it's been a 20% grower historically. And so I would expect it to continue to be a really strong grower that is above the portfolio average.

Matthew Philip Howlett
B. Riley Securities, Inc., Research Division

Got you. Great. And then just one last one, if I may. I mean Lugano is just an incredible investment, an incredible story. I don't know if you've done this in the history, but would you -- do you look at it as somebody you could sell a minority interest, bring in a partner, it's been -- it's so big, you could use it -- some flexibility to buy another portfolio company? Just do we -- how should investors look at this? I mean you have this at your hip pocket, this company that's growing phenomenally throwing off cash. I mean what can you tell us what you could do with it long term to create even more value than it already has for shareholders?

Elias Joseph Sabo
Partner & CEO

Yes, I think those options exist, Matt. The problem becomes -- it gets a little bit complex when you start bringing in third-party investors into our structure. And you got to look at kind of them benefiting from how we structure our deals by being the lender and the equity, which clearly performed so good at Lugano, do you really want to cut off that strip anymore?

So let's just -- suffice to say there's lots of opportunities. I think those opportunities create complexity. And in general, we're trying to create a little bit more simplification so that we're an easier story to understand, not harder. But that clearly is a benefit. And I would say given the growth rate of Lugano, and frankly, our forecast doesn't assume that it continues to grow at the pace that it has been. And there is upside. But it also manifests itself through far greater earnings per share.

And so I would hope that, yes, there's greater financing opportunities. But obviously, as our earnings grow, that creates just direct financing opportunities in the business, whether that be on equity financings or whether that be in debt financing. But yes, it will give a plethora of options. And having a company like this, which -- if you remember back, we had Fox Factory, which was an extraordinary investment for us, Lugano is an extraordinary investment. We've had a lot of them. BOA is in that same vein. But Lugano, just based on its sheer growth rate and mass at this point, it is a little bit unique, and we'll clearly think about what we can do to create even more incremental value from owning that asset.

Operator

And I'm showing no further questions. I would now like to turn the call back over to Elias Sabo for closing remarks.

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
This concludes Compass Diversified conference call. Thank you, and have a great day.