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RPM.N - Q2 2021 RPM International Inc Earnings Call

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OVERVIEW:

Co. reported 2Q21 consolidated net sales of $1.49b and adjusted diluted EPS of $1.06. Expects 3Q21 consolidated sales growth in mid-single-digit range.

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CORPORATE PARTICIPANTS

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

Matthew T. Ratajczak *RPM International Inc. - VP of Global Tax & Treasurer*

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

CONFERENCE CALL PARTICIPANTS

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

Frank Mitsch *Fermium Research, LLC - Senior MD*

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

John McNulty *BMO Capital Markets Equity Research - Analyst*

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

Kevin McCarthy *Vertical Research Partners, LLC - Partner*

Michael Harrison *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

Michael Sison *Wells Fargo Securities, LLC, Research Division - Senior Analyst*

Rosemarie Morbelli *G. Research, LLC - Research Analyst*

Silke Kueck-Valdes *JPMorgan Chase & Co, Research Division - VP*

Steve Byrne *BofA Merrill Lynch, Research Division - Director of Equity Research*

Vincent Andrews *Morgan Stanley, Research Division - MD*

PRESENTATION

Operator

Welcome to RPM International's Conference Call for the Fiscal 2021 Second Quarter. Today's call is being recorded. This call is also being webcast and can be accessed live or replayed on the RPM website at www.rpminc.com.

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

During this conference call, all references may be made to non-GAAP financial measures. To assist you in understanding these non-GAAP terms, RPM has posted reconciliations to the most directly comparable GAAP financial measures on the RPM website. (Operator Instructions)

At this time, I'd like to turn the call over to RPM's Chairman and CEO, Mr. Frank Sullivan, for opening remarks. Please go ahead, sir.

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

Thank you, Denise. Happy New Year, and welcome to the RPM International Inc. investor call for our fiscal 2021 second quarter.

Joining me on today's call are Rusty Gordon, RPM's Vice President and Chief Financial Officer; and Matt Ratajczak, our Vice President, Global Tax and Treasury, who is also supporting our Investor Relations activities.

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I'll take a few moments to provide an overview of the factors driving our strong financial performance for the quarter and also share an update on our MAP to Growth operating improvement program. Matt will then review our second-quarter financial results in detail. And then Rusty will wrap up with our formal remarks with an outlook for the third quarter of our fiscal 2021 year, after which we'll take your questions.

I'm very pleased to report that we generated record sales, earnings and cash flow for our second quarter. The excellent performance was achieved largely due to the efforts of our associates to grow our top line, which was achieved by three out of our four segments despite challenging economic conditions worldwide, coupled with operational efficiency improvement activities.

The MAP to Growth initiative once again generated strong leverage to the bottom line on moderate sales growth of 6%. Organic sales grew in a broad range of categories, including cleaning, disinfecting products, air purification equipment, small project paints, OEM coatings and other areas. Acquisitions also contributed to sales, including the second quarter addition of Ali Industries, which is best known for its Gator brand of abrasive products. Ali is the largest acquisition we made since fiscal 2013 and positively impacted both sales and earnings in the quarter, while also demonstrating our renewed focus to invest in growth initiatives.

Foreign currency translation also added to sales as international markets, particularly those in Europe, showed improvement. On an adjusted basis, our consolidated EBIT margin increased 240 basis points to 13.4% during the quarter, driven by three of our four segments registering substantial EBIT margin improvements and high EBIT growth. This was even more impressive given a tough comparison last year when adjusted EBIT increased 22%.

Our Consumer business continues to lead the way driven, by unprecedented consumer demand for its small project paints, caulks, sealants, stains and cleaners, while our other segments are finding ways to compete and win in the markets they serve. Our businesses remain focused on growth and are continuing to develop new, innovative solutions for our customers. One example is DAP's Eclipse Rapid Wall Repair Patch, which is just introduced and was developed to quickly fix most common drywall damage with simple, mess-free repair. Another is Carboline's Pyrocrete 341, a next-generation cementitious coating for passive fire protection. With enhanced application properties and excellent durability, Pyrocrete 341 positions Carboline as a market leader in passive fire protection.

In addition, our Construction Products Group recently introduced a suite of products that will keep us working this winter in temperatures as low as minus 20 degrees Fahrenheit, including AlphaGuard PUMA and Vulkem EWS waterproofing coatings, which are used to protect roofs and concrete. And, in a challenging construction market, our Construction Products Group continues to focus on renovation is exemplified by its Spectrem Simple Seal for façade restoration. On one recent residential tower in Minnesota, a complete window replacement was estimated to cost $15 million. Tremco won the job by recommending its Spectrem Simple solution, which was used to restore the site at a cost of only $1 million. We expect significantly more of this restoration product project sales.

Our MAP to Growth program continues to have tremendous momentum. During the second quarter, we announced the closure of two plants, which brings our total to 25 out of the 31 plants that were originally targeted for closure at the start of the program. We're also becoming much more efficient in utilizing our manufacturing assets as our focused improvement team meetings continue to deliver cost savings opportunities. One example is a Dryvit manufacturing engineer, recently trained in Six Sigma principles, who identified process improvements to reduce scrap and increase yields, which will result in $250,000 in annual savings. There are literally hundreds of other continuous improvement examples like this across RPM as we have invested in training our operations associates throughout the MAP to Growth program. In addition, the targeted benefits from our center-led procurement initiatives are ahead of plan, and our administrative improvements and ERP consolidations are continuing to be implemented.

As mentioned last quarter, we expect that we will reach the MAP to Growth programs planned run rate of $290 million of annualized savings by the conclusion of this fiscal year. That said, to our culture of continuous improvement, we continue to add to our robust pipeline of cost savings initiatives and operational improvements that will carry into fiscal '22 and beyond and will ultimately result in exceeding our original MAP to Growth expectations.

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Based on our improved margins and better working capital management, our business units generated record cash from operations, which increased 93% to $580 million. We've been strategic in managing this record cash flow, using it to pay down debt, make acquisitions and an increase in our cash reserve. At quarter end, total liquidity stood at $1.6 billion, making our balance sheet stronger than it has been in a long time.

One final comment I'd like to make relates to my predecessor, Tom Sullivan, who's also my father and mentor, who passed away on November 30. I share this because we had a tremendous influence on shaping the RPM of today. He took over the business in 1971 after his father died unexpectedly. At that time, RPM sales were $11 million. Following a 55-year career with RPM, Tom retired from our Board in 2016 when annual sales had reached nearly $5 billion. His leadership engrained practices within the organization to continue to perpetuate our growth and success, and his spirit continues to drive RPM.

I'll now turn the call over to Matt Ratajczak, who will review our fiscal '21 second-quarter financial results in more detail.

Matthew T. Ratajczak - *RPM International Inc. - VP of Global Tax & Treasurer*

Thanks, Frank, and good morning, everyone. Please note that my comments will be on an as-adjusted basis. During the second quarter, we generated record consolidated net sales of $1.49 billion, an increase of 6% compared to the $1.4 billion reported during the same quarter of fiscal 2020.

Organic sales increased 3.5%, or $49.5 million. Acquisitions contributed 2.3% to sales, or $32.6 million. Foreign exchange was a tailwind that increased sales by 0.2%, or $2.5 million. Adjusted diluted earnings per share were $1.06, an increase of 39.5% compared to $0.76 in the year-ago quarter.

Our consolidated adjusted earnings before interest and taxes, EBIT, increased 29.7% to $199.3 million compared to $153.7 million reported in the fiscal 2020 second quarter.

Turning now to our segment results, sales in our Construction Products Group increased 0.8% to $503.5 million compared to $499.5 million a year ago. Organic sales increased 1.2%, or $6.1 million. There was no impact from acquisitions. Foreign currency translation reduced sales by 0.4%, or $2.1 million. Adjusted EBIT in the Construction Products Group increased 26.8% to $78.5 million from adjusted EBIT of $61.9 million reported in the year-ago period.

The segment was able to leverage its modest sales growth into outstanding results on the bottom line, largely due to MAP to Growth initiatives, aggressive discretionary cost cuts and proactive management to improve its product mix. This was achieved despite soft commercial and institutional construction markets in North America and in Europe. The segment was able to maintain its top line by focusing on renovation and restoration projects, expanding its position as a single-source provider of building envelope systems and continuing to take market share with its industry-leading construction technologies, including its Nudura insulated concrete forms.

Sales in our Performance Coatings Group decreased 11.6% to $258.8 million from $292.7 million a year ago. Organic sales declined 12.2%, or $35.6 million. Acquisitions contributed $0.6 million, or 0.2% to sales. Foreign exchange increased sales 0.4%, or $1.1 million. The segment's adjusted EBIT was down 24.2% to $28 million compared to $37 million in the prior-year period.

Similar to last quarter, the Performance Coatings Group's sales continued to be impacted by Covid-19 restrictions that limited access to construction sites and also by weak energy markets that resulted in a deferral of industrial maintenance spending. Industrial capital spending has been restricted, especially in the energy sector, which is the largest market for our industrial corrosion control and fireproofing coatings businesses. The segment was particularly challenged in emerging markets. And its Carboline business was temporarily disrupted by hurricanes in the Gulf region of the U.S. The segment's earnings were impacted by declining sales, partially offset by MAP to Growth savings and discretionary cost reductions. Out of all of our segments, the Performance Coatings Group has been unfavorably affected the most by the pandemic. However, it also stands to benefit significantly from the pandemic's end, as its customers catch up on deferred maintenance and construction projects.

The unprecedented demand for our consumer products continued this quarter, resulting in a significant increase in sales for our Consumer Group. They increased 21.4% to $547.5 million from $450.9 million in the fiscal 2020 second quarter. Organic sales increased 15.2%, or $68.6 million.

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Acquisitions contributed $26 million, or 5.8% to sales. Foreign currency translation increased sales by 0.4%, or $2 million. Adjusted EBIT in the Consumer Group increased 65.8% to $90.7 million compared to $54.7 million in last year's second quarter.

Our Consumer Group's outstanding performance was driven by our broad distribution and by leveraging our market-leading position as homebound consumers tackled significantly more projects. We are investing in paint-making and aerosol filling capacity to help meet this demand. The top line also benefited from vigorous cleaning product sales, favorable translational foreign exchange and the acquisition of Ali Industries. Raw material costs were stable overall during the quarter. However, we are currently seeing broad-based inflation in a number of raw materials. High sales volumes and MAP to Growth savings were leveraged to the segment's strong bottom line.

Specialty Products Group sales were $176.1 million, an increase of 11.3% compared to $158.2 million in the year-ago period. Organic sales increased 6.6%, or $10.4 million. Acquisitions contributed 3.8%, or $6 million to sales. Foreign currency translation increased sales by 0.9%, or $1.5 million. Adjusted EBIT in this segment increased 27.7% to $29.6 million this quarter compared to $23.2 million in the second quarter of fiscal 2020.

Management changes that we implemented at the Specialty Products Group have helped to turn around results of the segment this quarter. Sales were boosted by increased hurricane and wildfire activity, which drove demand for our water restoration equipment as well as fluorescent pigments, which are used in fire retardant tracer dies. Additionally, we continue to experience strong demand for our expanding product lineup of disinfectants, air purification equipment and HEPA filters. Several of this segment's end markets have improved. For example, sales of its industrial wood protection products increased as a result of improved lumber demand in the U.S., and we have expanded sales in our forestry chemicals business in Australia and New Zealand. The segment's bottom line increased as a result of higher sales volumes, operational improvements and MAP to Growth savings.

Now, Rusty will walk you through our outlook.

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

Thanks, Matt. As we look ahead to the fiscal 2021 third quarter, we anticipate consolidated sales growth in the mid-single-digit range with continued strong leverage to the bottom line from our MAP to Growth program, resulting in adjusted EBIT growth of 30% or more. Our third quarter typically provides relatively modest sales activity each year because it falls during the winter months when painting and construction activity slow. As a result, there is typically greater volatility in percentage terms given the unpredictable weather. Also, this seasonal reduction of activity will benefit our Consumer Segment, enabling it to replenish retail inventories after working to meet unprecedented demand over the last six months.

From a segment perspective, we expect fiscal 2021 third-quarter sales to be flat to negative in the Construction Products Group. This group will continue to outperform its peers in a challenging construction market by continuing to focus upon building restoration and renovation with innovative products and service solutions. We expect the sales decline to continue in the Performance Coatings Group, which serves the most challenged end markets at RPM. We expect the Consumer Group to continue to leverage its market-leading position into double-digit sales growth due to a number of factors, including: number one, continuation of strong POS results; number two, more shelf restocking after retail inventories have dropped due to unprecedented demand; and number three, continued benefit on both the top and bottom line from the Ali acquisition, which is performing better than we anticipated. We expect positive sales growth from the Specialty Products Group to continue into the third quarter as well. New management has brought fresh ideas and processes for business development, and their OEM customer base has recovered as manufacturing has picked back up from the shutdowns last spring.

Additionally, RPM's cash flow has soared to new highs due to margin improvement and better working capital management, as well as the unprecedented consumer demand, which has drawn down our Consumer inventory. A portion of this working capital reduction will not be sustained since we will need to rebuild Consumer Group inventory.

Across all of RPM, there's still much work to do to improve our manufacturing flexibility and planning processes that will help us simultaneously serve our customers while reducing the necessary safety stock levels. Sales in all four segments should be up in the fiscal 2021 fourth quarter due to an easier comparison to last year's fourth quarter, which is when the economic interruption caused by the pandemic was most severe.

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With recent optimism surrounding the vaccines for Covid-19, let me spend a moment to tell you about what life getting back to normal means for our four segments. For Consumer, we would expect DIY activity to return to more normalized levels as people venture out of their homes. But we still anticipate elevated demand due to the expectation of continued low interest rates, good housing turnover, an expanded end-user base since more DIYers have recently entered the category, and our Consumer pro business picking up again as contractors gain access more often to residences. We also believe that cleaning is an area of greater consumer interest as we go forward.

For our CPG and PCG segments, getting back to normal will improve facility access for our contractors and likely improve construction activity from what has been a challenging 2020 calendar year. We would also expect a boomerang effect in the future as deferred maintenance catches up. For those who followed RPM in the last Great Recession, you'll recall that our former Industrial Segment experienced double-digit growth in 2011 and 2012 from the catch-up of deferred maintenance. For SPG, we continue to rebuild growth momentum under the new management team.

Due to continued economic uncertainty related to the impacts of Covid-19, we are not providing fiscal 2021 full-year earnings guidance.

This wraps up our formal comments. We will now be pleased to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from John McNulty with BMO Capital Markets.

John McNulty - *BMO Capital Markets Equity Research - Analyst*

First, my condolences to you and the RPM team with the passing of Tom, who obviously left an amazing legacy behind.

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

Thanks, John.

John McNulty - *BMO Capital Markets Equity Research - Analyst*

For sure. So, I guess the first question, because we've obviously seen some inflation in some of the raw materials, and you made mention of it in some of the prepared remarks. Can you speak to the type or level of inflation you expect to see as you work through the rest of your fiscal year? And also speak to the ability that you have to price it through so you can offset some of those headwinds in a timely fashion.

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

Sure. So we're seeing some challenges in areas like silicones, epoxies, metal cans and certain other raw material categories. We fully expect to offset those initially through the continuing benefits of our consolidated procurement activities, which have been providing, I think, leverage and benefits beyond what our original MAP to Growth expectations were. And then while we're very stable in terms of pricing now, I think it's highly likely that you'll see across our industry some price increase activities this spring.

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John McNulty - *BMO Capital Markets Equity Research - Analyst*

Got it. Fair enough. And then I guess, you've got a number of new growth initiatives. You've got some grab-and-go programs coming on. You made mention of some of the investments even in the new paint capacity. Can you speak to how programs are going at this point in terms of the growth and your expectations, and also how you're thinking about the investment needed to drive these businesses?

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

Sure. Number one, we are making the investments needed to drive these businesses as we speak today. We expanded capacity in Consumer in a number of categories. We're also expanding capacity in our Construction Products Group. And we are making a not-so-subtle shift in our MAP to Growth activities to the growth aspect of it. I think you can see that most pronounced in our Construction Products Group, which actually had modestly positive organic growth in this quarter in a very challenged end market pretty much globally. And they have shifted to some major restoration activities. The combination of our Dryvit business, Nudura, the Tremco Roofing and Tremco Sealants and the spec efforts are paying big, big dividends, and we would expect more of that to come, particularly in any type of construction activity rebound. And so, you're seeing that -- we mentioned a few of the new product categories today. We are keenly focused on driving organic growth in the coming years. And at the same time, I think Rusty made reference to the fact that we would expect MAP to Growth, which is exceeding our expectations, to continue to deliver additional savings as we get into fiscal '22.

Operator

Your next question comes from Rosemarie Morbelli with G. Research.

Rosemarie Morbelli - *G. Research, LLC - Research Analyst*

And again, I will join on my condolences regarding Tom's passing, Frank. We are all terribly sorry, and I worked with him for many years, more than I'd like to think about. Looking at your investments, what -- which particular product lines are you thinking of growing? I mean, do you -- let me rephrase this. Which product lines are you investing towards additional capacity in your different businesses?

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

Sure. In Consumer, we are investing in small project paint capacity and aerosol capacity. We're also looking at gallon goods and capacity in caulks and sealants, so pretty much across the board. We're also expanding capacity in cleaning product categories. In our Construction Products Group, we are expanding capacity in roof restoration coatings across a whole broad spectrum of areas, and we're expanding capacity in façade restoration projects. So that ranges across Nudura, Dryvit and Tremco Sealant unique product categories.

We're also expanding capacity in a number of Specialty Products Group businesses, particularly Legend Brands in terms of their capacity for air filtration and air handling and restoration equipment. About the only area that we're not expanding capacity at this point is in our Performance Coatings Group, given the impact of the pandemic and oil and gas prices on some of their major product categories.

Rosemarie Morbelli - *G. Research, LLC - Research Analyst*

Do you see a need to eliminate some capacity on the Performance Coatings as some categories may not go back to the pre-Covid level?

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

We would fully expect categories to get back to pre-Covid levels over the next coming years, and that's been our history in the past. I will tell you we had been eliminating capacity across RPM as we highlighted in our prerecorded -- or our formal remarks. We completed the closure of 25

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manufacturing facilities. And I believe by the time that we're finished, we will exceed by a few the original 31 plant closures that we targeted in MAP to Growth. And so, we're having a very deliberate reallocation of capital into growth areas and into efficiency. So, while we're expanding capacity by the time we're done with MAP to Growth, our net manufacturing footprint around the globe will be smaller.

Rosemarie Morbelli - *G. Research, LLC - Research Analyst*

And I was wondering if you could make some comments regarding your efforts towards adding architectural paint to your portfolio.

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

Sure. We have commented in the past about a number of kind of unique category architectural paint opportunities that we've had across a number of our major customers. And in that, I think we'll have a better sense of that this spring and this summer as we get through kind of the post-Covid supply challenges across numerous areas in the consumer DIY market.

Operator

Your next question comes from Frank Mitsch with Fermium Research.

Frank Mitsch - *Fermium Research, LLC - Senior MD*

Congrats on the quarter. More importantly, Frank, let me add to the condolences. I mentioned before that I thought your eulogy was one of the best I ever heard, what an amazing man in life. And on a happier note, congrats on your Browns, and good luck on -- I don't know if it's Saturday or Sunday, but be nice to take care of the guys in Pittsburgh.

You spoke a little bit about cash generation, record free cash flow and your strategic uses. I didn't hear much with respect to buybacks and when might they resurface and/or what your pipeline is looking like on the M&A side. How do we think about the interplay for RPM on M&A versus buybacks?

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

Sure. So, cash generation is at record levels, and it will continue that way for the foreseeable future, combination of margin expansion, the capital allocation strategies we're deploying, as well as just excellent working capital improvements. For the time being, we have indicated that we had suspended our share repurchase program in favor of debt reduction. We've been able to affect some meaningful debt reduction. Going forward, the pipeline of M&A activity in our industry is pretty full and growing. So, we continue to pursue our typical small- to medium-size acquisition activity. And I think over the next 12 to 24 months, you'll see more transactions like the Ali Industry transaction we completed in the second quarter. As it relates to share repurchases, that's something that our Board will take up in board meetings here this winter and this spring.

Frank Mitsch - *Fermium Research, LLC - Senior MD*

Got you. Got you. Obviously, the Consumer business has been a standout, very strong sales. You mentioned that you're going to take the opportunity during the fiscal third quarter to rebuild inventories. Were there -- did you lose any sales, you think, on the consumer side because you were sold out? Could the results have been better? How do we think about what could have been in that regard?

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

Yes. Clearly, we have lost some sales relative to fill rates. It's not unique to us. It's impacted many DIY categories. As people know, in our first quarter, we had organic growth in Consumer of 34%. We had organic growth in the second quarter in the mid-teens. We continue to see strong organic growth. And certainly, there were some opportunities for us for additional growth had we been able to fill orders at a higher rate. As Rusty commented in our -- and Matt comment in our prepared remarks, we see catching up on a lot of that activity in the third quarter. And I think we remain very bullish about both our position in the DIY market and where the DIY market will continue in terms of pretty strong growth for the foreseeable period of time in calendar '21.

Operator

Your next question comes from Ghansham Panjabi with Baird.

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

Happy New Year! And Frank, my best to your family as well. So just given that your quarter ended in November, obviously, lockdowns have picked up in Europe since then. Can you just give us a sense as to how things have progressed in December, what they're tracking like in early January across your businesses? And if anything is different from the pre trend line specific to the first lockdown across your businesses.

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

Thank you. Sure. That's I think a great question because the possibility exists for a lot of variability in our Q3. We are off to a great start. Organic growth continues across our different businesses at the beginning of the third quarter. Leverage to the bottom line has been tremendous. And we would expect to meet or exceed the forecast numbers or the guidance numbers that Rusty provided in the formal comments that we made. What could interrupt that is further lockdowns. The U.K. has locked down into mid-February, as you know. If that is followed by lockdowns throughout Europe, and then back in the United States, certainly, that could disrupt what otherwise would be another very strong quarter for RPM.

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

Got it. And then in performance in your call out for deferred maintenance in the energy sector, can you give us a sense as to how that dynamic impacted you specific to the 12% sales decline you reported in the second quarter? And what's reasonable in terms of the catch-up phase because I assume you can't defer it for too long?

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

Sure. I think the best way we can address that again was in the prepared remarks that Rusty made. We look back at calendar 2011, 2012, and we generated double-digit organic growth in our Performance Coatings Group businesses and our Construction Products Group businesses on the rebound. And certainly, in the Performance Coatings Group area, the negative impact, particularly in oil and gas, energy and heavy industry spending has been as severe as it was back then. And so, we would expect a meaningful rebound in those categories on any economic recovery activity.

And so, I think we're really well poised there. And you'll see in the coming quarters, the benefits of the MAP to Growth activity on our Performance Coatings Group. In this quarter, their earnings performance was negatively impacted by some unique circumstances around the hurricanes and weather activity that impacted the Gulf in their major manufacturing facility in Lake Charles, Louisiana. So, part of that earnings performance was circumstantial to the quarter. So, we're really pleased with where they are.

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The Construction Products Group, I think, has the opportunity to really drive our performance into fiscal '22. We are taking market share. We are introducing new product categories. We are combining prior independent businesses to attack façade restoration on a holistic basis. And so, there's a lot of exciting things happening there that, again, we would expect to see accelerate in any type of economic recovery.

Operator

Our next question comes from Vincent Andrews with Morgan Stanley.

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

If I could just follow-up on the Consumer business, a couple of questions. Are you noticing within the DIY customer that the product mix that they're purchasing is evolving to the extent that maybe there's sort of a life cycle where people that were early in DIY were doing certain types of projects, and now six months later, they're doing different types of projects, but you're seeing a new cohort come in at sort of at the earlier stage? Or just sort of any evaluation of the trend you're seeing that can help us understand your confidence and sort of the sustainability of this into the next fiscal year?

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

Sure, both in terms of what we've experienced and what we've heard from our major customers, the base of confident DIYer has expanded pretty significantly. And certainly, in ways neither we or big customers could have accomplished in normal circumstances on our own. And a good example of that is our wood stains and finishes businesses had the same type of robust organic growth as our small project paint business. And that requires some more craftsman skills and they're larger projects. And so, I think we're all pretty confident that this larger base is here to stay and that we can grow from there.

The one area that was meaningfully negatively impacted was the pro. And so that might be 20% to 25% of our Rust-Oleum small project paints and cleaner categories, but closer to 40% or 50% of our DAP caulks and sealants and patch repair products and our Zinsser primers. And pro contractors have been inhibited from getting access to residences, to the interior of residences, where most of our products are applied, as well as its impact on some kind of small project, like commercial restoration. So, we see that business coming back strongly once people have more confidence in putting the Covid pandemic behind us.

And then the last comment I'll make are new categories that we've been testing. We have had three different opportunities, which are still ongoing to test new programs in architectural paint. And so, you put all that together, and we're pretty bullish about our Consumer business through this pandemic period.

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

Okay. And if I could just ask a follow-up on the Ali acquisition. You mentioned that it's proceeding better than projected. Is that both on the top line and from a synergy perspective? Or just any incremental color you could provide there would be helpful.

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

Yes. It's both on the top line and what we're able to do with that business. Post MAP to Growth, RPM can bring some more immediate value to businesses that we acquired. Our manufacturing and operations folks have been working with Ali on a look forward for three years in terms of some manufacturing capacity expansion and also some automation efficiency improvements, so we're excited about that. And the ability to take advantage of the sales and marketing expertise at Rust-Oleum, which I believe is as good as anybody in the entire DIY space across any category, is pretty exciting as the Rust-Oleum sales and marketing folks marrying up with the Ali folks in terms of new opportunities and approaches.

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

And I'm sorry for your loss.

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

Thank you.

Operator

Your next question comes from Kevin McCarthy with Vertical Research.

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

Frank, did you have any businesses where price declined in the fiscal second quarter? And then looking ahead, as raw material costs come up, as you described, where would you say you're most confident in the ability to pass along those increases? And where you think it could be more challenging?

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

Sure. We've had a period of price deflation that we benefited from as well as the benefits of our consolidated purchasing activity, which is going quite well. We have not had meaningful price givebacks in any category across anywhere at RPM. In terms of price increases, we've had some very modest price increases in some very unique categories that aren't big enough to move the whole needle.

Going forward, as I mentioned, this spring and this summer, with the product categories that are most likely to be driving price increases across a number of our businesses are in packaging, especially as it relates to metal cans as well as in a number of chemical areas, depending on how things transpire in the coming months in the areas of silicones, epoxies, acetone, number of categories that are seeing price increases as we speak for the first time. It's worth keeping in mind from an RPM perspective, we're one of the few, particularly in the U.S., on FIFO accounting. So, the impact of these wouldn't hit our P&L for probably 60 to 90 days versus a lot of our peers, and we have the ability to both lead in some categories, but also follow-on others in terms of what's happening in price increases across the market.

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

Okay. And then in terms of -- I guess, what I was trying to get at, Frank, is your ability to raise price to your customers and pass that along. Are there any areas that you would call out where you already may be out in the market with proposed increases, for example?

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

Yes, we do not have any price increases in the marketplace today. I anticipate price increases in the future. And our ability to pass on price is consistent with what it's always been, relatively timely in our industrial businesses and typically, with a 6- to 12-month lag in our consumer DIY businesses. I think some of that will be tightened just because of where we sit with a few product categories. But we have passed on price appropriately in the past. You can see that in our margin expansion throughout this period. And I don't see anything that changes those dynamics, both on the plus side, which is our ability to ultimately pass on price, and on the lag side in terms of the delay in timing that we've experienced for decades in our consumer DIY businesses.

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

And then secondly, if I may, in Consumer, Frank, what is the level of the inventory that you need to replenish? And what impact could that have on sales and/or margins in what's normally a seasonally weaker quarter for the business?

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

Sure. I would expect really strong performance out of Consumer in our third quarter unless there is, as referenced earlier, some type of significant Covid impact, which would impact everybody. But we anticipate continued strong performance there and into Q4 as well. Rusty referenced working capital in Consumer. Certainly, we have tens of millions of dollars, low tens of millions of dollars of inventory to catch up on. And I think that's a good news story as well for the coming quarters.

Operator

Your next question comes from Josh Spector with UBS.

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

Just a follow-up from a prior question quickly. Are you able to size the hurricane impact in Performance on the top and bottom line in the quarter at all?

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

Well, I don't have those details. I don't know if we have them. Rusty, is that something that you might be able to comment on?

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

Yes. In terms of unusual expenses, there was a few million dollars of expenses. And in terms of sales, there was disruption from 3 hurricanes that have passed either right through Lake Charles or nearby in the second quarter. So that did disrupt not just our plant but our customers in the Gulf region. So yes, there was some sales impact that definitely played into the decline you saw at PCG.

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

Yes. That's why I mentioned in my comments, it was circumstantial to the quarter and actually despite the very challenged end markets, the MAP to Growth benefits on the PCG segment pretty pronounced, and I think you'll see those in the coming quarters in a positive way.

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

Okay. Yes. I guess what I'm trying to think about around this is you had 12% declines in Performance in both of the last 2 quarters. Is there a way to think about like what the exit rate was or what the normalized demand was as we start to look at the next quarter and think about the recovery over the next couple of quarters?

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

No, I think you'll see the positive results as we get into our fiscal '22 in part because they'll be annualizing easier comps. But I do think with any economic recovery, there's a significant amount of pent-up maintenance and heavy industry spend that we'll be the beneficiaries of.

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I guess the last comment I'll make is if you look at what we expect in Q3 and Q4 out of that segment, I think you'll get a better sense of the positive impact of MAP to Growth even as revenues continue to be down year-over-year or flat. And it will give you a better sense from a margin profile of what type of leverage we would have when positive sales results return.

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

Okay. I appreciate. That's helpful. And just one last quick one, if I can, just on MAP to Growth and the savings that you expect to realize. I mean, you reiterated your run rate savings target here. Are you able to quantify how much savings you expect to be realized in fiscal '21 versus fiscal '22 at this point?

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

Yes. I'll defer that to Rusty other than to say that we're highly confident that some of our ability to execute timely has been impacted by the Covid pandemic. But we're highly confident that as we get into fiscal '22, we'll continue to benefit from our MAP to Growth activities that the total program savings will be well in excess of $300 million.

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

Yes. And Josh, as we said on the last call, we expect $100 million or more of MAP savings to favorably impact FY '21.

Operator

Your next question comes from Arun Viswanathan with RBC Capital.

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

My condolences to you as well. I guess I just wanted to first ask about the Consumer Segment, the margin performance. If you think about it, Q1 '21 to Q2 '21, you had about close to 500 basis point margin drop-off in EBIT percent. Obviously, there's a lot going on in there. But how would you kind of characterize that performance? Do you feel that the Consumer Segment was potentially impacted by some of those stock outs and you see the margins kind of recovering to higher levels in subsequent quarters?

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

Sure. Let me address that broadly, and then Rusty can address it in some detail. But all of our businesses, particularly our Consumer businesses are seasonal. And I think if you look year-over-year, we're continuing to see significant margin expansion. But obviously, from one subsequent quarter to the next as we get into our fourth quarter and first quarter, which are absolutely our seasonal highs, and our second quarter and third quarter are meaningfully less in revenues, and there's a fixed level of expense. So that's what's driving the margin differential quarters over subsequent quarter, but we've continued to experience significant year-over-year margin improvement, and we would expect that to continue. And I think Rusty could add a little more detail to that.

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

Yes, that's correct, Frank. Yes, as we get into cooler months in the fall, sales typically fall off as they normally do. So, the fact that we had stronger sales and more leverage on fixed costs, Arun, would naturally lead to a higher margin in Q1 and Q2. But when I look year-over-year, Consumer's up 450 basis points in EBIT in Q2. So, I think we're doing pretty well.

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

Agreed. And then on Construction Products, you guys alluded to potential opportunities coming your way to gain share. Do you believe that there is inorganic additions you have to make to your portfolio to capitalize on that? Or could you potentially capture that share through some of these investments you've described as well?

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

So I believe we can and are capturing that share through the activities that we've taken as we speak. There will be inorganic opportunities in that category, broader opportunities that may appear, but on a pretty regular basis, product lines that we can acquire and expand across our distribution base. But fundamentally, what happened in our -- by going from our former six groups into four groups and four segments, we have consolidated a number of businesses more completely into a more comprehensive Construction Products Group. And so, while we operated across the globe with maybe five or six different business units, we are now operating in North America and in Europe as a Tremco Construction Products Group. And pulling together, for instance, Tremco Sealants, the Nudura and the Dryvit businesses, and approaching the market on an integrated basis is opening up opportunities for us in façade restoration that is driving organic growth, that we were not experiencing the way we were organized in the past.

So, the biggest part of it has to do with reorganizing into a more integrated $2 billion Construction Products Group, which from a market perspective, is the Tremco Construction Products Group on a pretty integrated basis. We have exceptional leadership there, and we continue to take market share, whether it's in add mixtures shifting from different business units into a more integrated approach to the marketplace and something we're really excited about. There will be inorganic acquisition opportunities to accentuate that as well, but we do not need those to keep driving market share gains and organic growth.

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

Okay. And then real quickly, lastly, on the raw materials front, do you foresee any categories, things specifically like MMA and/or epoxies where you potentially could face some supply chain disruptions or availability issues that you're concerned about? Or do you feel okay with the overall level of inventory that you have in your raw material procurement?

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

So we have, over the last few quarters and months, faced some challenges in certain packaging areas and particularly in metal cans. We have faced some challenges in silicones. A lot of those categories in terms of availability are being cleaned up. So, I don't think we have the same concerns going forward as we've had over the last couple of quarters in those categories. And so, I think that's certainly an observant comment about what's happened in a couple of categories, particularly for us in some packaging areas and silicones.

Operator

Your next question comes from Mike Harrison with Seaport Global.

Michael Harrison - *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

Our condolences to you and your family, Frank. You mentioned the management change that occurred in the Specialty Segment and talked about some new ideas, new processes around business development. Can you give a little more color on what changes have been made there and your confidence in sustainability of improving results in that business?

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

Sure. We have a new segment leader who's been in charge of that group for just about two years. And Ronnie Holman has done a great job. Ronnie started as a leader of our R&D effort in a $15 million wood coatings businesses that was acquired by RPM probably 30 years ago and helped grow our OEM coatings businesses to nearly $300 million and is now in charge of this larger group. We have new leadership at DayGlo. We have new leadership coming at our Mantrose-Haeuser business. We have reorganized a new leadership across our ValvTect and Pettit Marine business and really excited about what's happening there. And so, there's been a number of leadership changes there that consolidated accounting administration, not only from a cost perspective, but to take those administrative functions away from essentially business leaders that are refocused on growth.

We have also changed our mentality at RPM under my father, Tom and his partner, Jim Karman, for decades. We just did not use outside consultants. We've had a lot of success, both with our teams and the good work of some consultants in the MAP to Growth program. I mention that because something that we would not have done in the past we are doing today. We hired McKinsey to work with our DayGlo team and our Mantrose-Haeuser specialty food business teams, focused on market sizing and market opportunities. So, the shift that I mentioned earlier in terms of really focusing our businesses on growth as well as sustaining and implementing the MAP to Growth cultural changes with RPM are happening.

And I think the thing that we're most excited about, big picture, our primary goal on MAP to Growth was to get efficiencies that were there to have to change our culture to be focused not only on growth but on efficiency, but do it in a way that did not meaningfully, negatively impact our entrepreneurial culture. And so far, we have been able to do that. And it's paying dividends, and I think people are going to see that in the coming quarters across our pan particularly in the Construction Products Group and particularly in our Specialty Products Group.

Michael Harrison - *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

All right. That's very helpful. And then also I wanted to ask about the online sales portal or your online sales effort. That was an area that you were kind of struggling with last season. I was wondering if you've made some changes or progress in those online sales that should enable you to better leverage potential demand to the bottom line as we get into the busier season in 2021?

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

Sure. And again, Rusty may have some more detail. I could tell you, particularly in our Consumer Group, our ability to service online ordering has improved dramatically. And we have seen significant improvement and huge percentage gains, but they're on a small base, but improvement in our ability to fulfill and meaningful, meaningful growth in some of our big box customers and more on traditional online customers like Amazon.

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

Yes. Our growth in online sales is not quite double, but it's probably up close to 80% this year. And your question is very perceptive because we are focusing a lot of our operating improvement team initiatives in the area of distribution. So, I think we're going to continue to improve that this year because you're right, the landscape has shifted.

Operator

Your next question comes from Mike Sison with Wells Fargo.

Michael Sison - *Wells Fargo Securities, LLC, Research Division - Senior Analyst*

My condolences to you, Frank, as well. And I just wanted to say, I always enjoyed meeting with Tom during the solid days back, and then those were always fun meetings, but just one quick question. The first half of '21 free cash flow was above $500 million, and it looks like you'll generate

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some free cash flow in the second half of the year. So, is this sort of $600 million plus type free cash flow potential kind of the right run rate that RPM can generate on an ongoing basis going forward?

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

Yes. Big picture -- and again, details, I'll turn it over to Rusty, but big picture, I think we have gotten RPM to a new level of cash generation, both in terms of working capital requirements on a go-forward basis as well as our margin profiles, and we're excited about that. I think Rusty can provide more details as it relates to fiscal '21 and beyond.

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

Sure. Yes, you might remember, Mike, on Investor Day, we showed a slide that said our cash from operations, our target was $872 million, I believe. And if you look over the last 12 months, we're running over $800 million of cash flow from operations for the trailing 12 months. So, we're pretty close to that. If you look at the dividend and the capital spending, this year we'll do over $140 million of capital spending. I think the dividend is pushing close to $200 million. So, to answer your question on free cash flow, at the rate we're running, yes, we're certainly over $400 million of free cash flow.

It's hard to take the last 12 months as any guide for what normal is because of the pandemic. For example, we have deferred some government payments for about $25 million, including the payroll tax. We have drawn down inventories, but other businesses, as we discussed, are suffering because of the pandemic. So, it's tough to use the last 12 months as a guide, but we appear to be tracking towards that MAP target.

Operator

Your next question comes from Steve Byrne with Bank of America.

Steve Byrne - *BofA Merrill Lynch, Research Division - Director of Equity Research*

Can you quantify how much discretionary spending cuts were in the quarter? And what portion of that might reverse?

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

Yes. I'll defer that in detail to Rusty again. But big picture, we have had some meaningful reductions in discretionary spending that's associated with the pandemic that will come back. I can tell you that you'll see, and this is part of our guidance, a more normal spend in our Consumer Group in terms of advertising and promotion in the third and fourth quarter and the spring. So that's already coming back in part of our outlook. And while some of it will return, part of it was just lucky in terms of coinciding with our MAP to Growth activities because across a number of our businesses, there will be a kind of a new level of discretionary spend that will be below probably even where we originally targeted in MAP to Growth.

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

Yes. In terms of the biggest area of spend is travel cost. So, we're probably saving somewhere around north of $10 million a quarter in travel cost. And like Frank said, we're -- with the new world we're in today, we're finding that we can accomplish a lot of things without travel, with video conferencing. So, I don't think necessarily all of that will come back. In the spring, we talked about medical costs going down because nobody went to the doctor. That's been back to normal this year. So that's another area you might be interested in.

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Steve Byrne - *BofA Merrill Lynch, Research Division - Director of Equity Research*

And since you brought up MAP to Growth in that response, I just wanted to drill into that on a couple of fronts. One being, how much of that $300 million target or maybe what you can say, how much of the savings you've achieved so far were from MAP to Growth? Would you say this arisen from lower raw material costs?

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

Rusty, you can check me on this. I would say I don't know, $50 million or $60 million is maybe lower raw material costs and the balance is from our specific activities. The -- and that certainly is part of a centralized procurement function that in combination with lower raws has exceeded our expectations. And then the other area that we've commented on was our original target for manufacturing operations between plant consolidation and efficiency gains was $75 million, and we'll exceed $100 million in that category.

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

Yes. I think the question might be about the commodity cycle assumption in MAP, and we assumed $145 million of procurement savings. And we said, I believe, $65 million in wave three would be related to the commodity cycle.

Steve Byrne - *BofA Merrill Lynch, Research Division - Director of Equity Research*

Yes. So, it's similar to you, Frank -- Rusty?

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

Yes. Yes.

Steve Byrne - *BofA Merrill Lynch, Research Division - Director of Equity Research*

And then just one last one for you, Frank. As you close out this MAP to Growth initiative, is it reasonable to think that you might introduce kind of the next plan, anything that you have learned from this initiative that might lead you down a new path of productivity initiatives?

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

Sure. We'll -- I think we'll be in a better position to address that with some specifics in July when we talk about guidance for fiscal '22 and kind of maybe a longer-term post-MAP to Growth outlook. But clearly, there are elements of the MAP to Growth program that are here to stay. The MS-168 element of manufacturing operations, our ability to be a more strategic partner to large global suppliers and what we're doing on the sales front as well are something that we'll be able to talk about.

And we've been able to put in procedures. This is a little in the weeds, but what came out of MAP to Growth was a very detailed, what we call MPGT, which is -- or MPGT, which is the -- I'm sorry, MPST, which is the MAP Project Savings Tracker. And so, we've been able to track literally thousands of categories of savings across procurement, across SG&A and efficiency, and we are taking some of those disciplines into a growth process as well, and we'll be able to talk more about that, both in terms of what we're doing and the impact it's having this summer.

Operator

And your last question comes from Silke Kueck with JPMorgan.

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Silke Kueck-Valdes - *JPMorgan Chase & Co, Research Division - VP*

I'm also old enough to remember Tom Sullivan. And so, I'm sorry to hear about his passing, but I'm glad I got to know him.

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

Thank you very much.

Silke Kueck-Valdes - *JPMorgan Chase & Co, Research Division - VP*

I have two questions. One on the Consumer Segment and one on the Construction Segment. In the Consumer Segment, is there a way to quantify just in ballpark terms, what's the benefit of Covid-related sales may have been in the quarter? Like, whether it's something that's like $10 million or something that's mid-single digits? Or is there any way to think about it?

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

Well, Rusty might have a better answer than I do. The only thing I can tell you is, historically, solid organic growth in Consumer has been in the 5% or 6% range. So clearly, a 34% organic growth in the first quarter and mid-teens organic growth in Q2 is extraordinary relative to historic levels.

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

Yes. I think the best way to think about it, Silke, is to look at the comp store sales numbers out of Lowe's and Home Depot. And they've been running over 20%, and you could compare that to a more normalized base. I think that would be probably the best way to think about it.

Silke Kueck-Valdes - *JPMorgan Chase & Co, Research Division - VP*

Right. And that leads to sort of a follow-up question on Consumer in that as Lowe's has been out thinking about like the year ahead on a calendar basis. And I think their view is that the U.S. home improvement market may be down, I don't know, 5% or 7% in calendar 2021. Is that the way you see it? And it's sort of like you see it like a similar alignment for RPM and for the Consumer business specifically?

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

Yes. First of all, that is not how we see it. We would expect to see continued double-digit growth in the first part of calendar or first four or five months of calendar '21. And then I expect, from what we're seeing to see positive growth rates for the balance of the year. In Lowe's perspective that you referenced is not universal across our customer base. We have some significant customers that see continued expansion in the DIY market, albeit at a lower pace.

Silke Kueck-Valdes - *JPMorgan Chase & Co, Research Division - VP*

Okay. Helpful. And my question on the Construction Segment is that the margin improvement in the Construction Segment has been pretty high with the MAP program, even though the sales growth has been slow. And the fourth quarter is typically the largest quarter for the Construction Segment. And the comparisons are relatively easy, as you pointed out. And so, like do you think that, that business in the fourth quarter can approach margins that are something like 20%, if you all of a sudden had good volume growth?

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

Sure. I'm going to give you a dodge on that question for two reasons. Number one, we really aren't providing detail on our fourth quarter, and we'll do so in April. But secondly, it's really going to be hard to tell. We had -- we should have some easier comps, particularly in April and May. As you see in this quarter, the leverage to the bottom line out of our Construction Products Group is pretty extraordinary. And I would expect that leverage to continue, at least directionally in what you're talking about. When they start to post organic growth, it's in the mid-single digits, which a recovery is coming.

Operator

And now I'd like to turn the call back over to Mr. Sullivan for closing remarks.

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

Thank you. As always, I'm grateful for the hard work and dedication of our associates around the world. It's through their efforts that we found ways to safely operate our businesses, meet our customers' needs, develop new innovative solutions and serve the communities in which we operate. I also greatly appreciate our shareholders for their continued investment in RPM. We remain focused on generating long-term value for you. We learned over decades that the market values growth over efficiency. And what we've learned in MAP to Growth is that we can do both, and we expect to continue to do both.

Finally, to everyone on the call, I wish you and your families a happy and healthy New Year. We look forward to updating you on our fiscal 2021 third-quarter results in April. Thank you for your investment in RPM and for joining our conference call this morning. Have a great day.

Operator

This concludes today's conference call. You may now disconnect.

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