

The Scotts Miracle-Gro Company

NYSE:SMG

FQ2 2021 Earnings Call Transcripts

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S&P Global Market Intelligence Estimates

	-FQ2 2021-			-FQ3 2021-	-FY 2021-		-FY 2022-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	GUIDANCE	CONSENSUS
EPS Normalized	5.57	5.64	▲ 1.26	3.57	9.00	-	9.14
Revenue (mm)	1732.94	1828.80	▲ 5.53	1443.35	4568.56	4100.00	4586.81

Currency: USD

Consensus as of May-05-2021 1:43 PM GMT

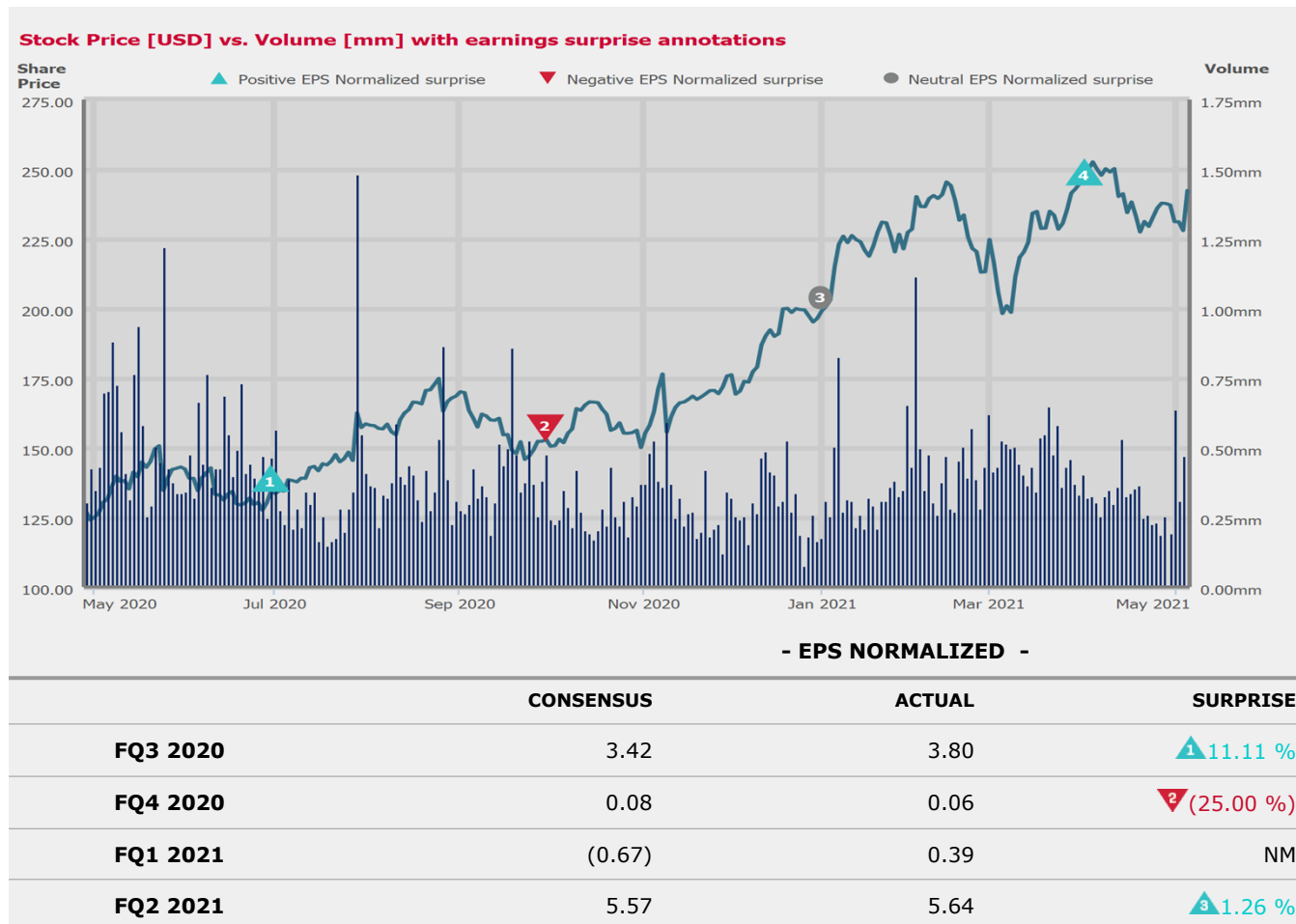


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Presentation

Operator

Good day, and welcome to The Scotts Miracle-Gro Company's second quarter earnings conference call. As a reminder, today's call is being recorded.

At this time, I would like to turn the conference over to Jim King. Please go ahead.

James D. King

Chief Communications Officer & Executive VP

Good morning, everyone. I'm Jim King, and I'd like to welcome you to the Scotts Miracle-Gro second quarter earnings conference call. Joining me this morning is our Chairman and CEO, Jim Hagedorn; our Interim Chief Financial Officer, Cory Miller; as well as our President and Chief Operating Officer, Mike Lukemire; and Chris Hagedorn, Group President of Hawthorne. In a moment, Jim and Cory will share some prepared remarks, and then we'll open the call to your questions. [Operator Instructions]

I've already scheduled time with many of you after the call to fill in the gaps. Anyone who wants to set up some Q&A time can call me directly at (937) 578-5622, and we'll work to set up some time as quickly as we can.

A quick bit of housekeeping. Cory and I will be participating in the William Blair Growth Stock Conference in early June, which once again will be held as a virtual event. As many of you know, historically, we've used this event as an opportunity to update the investment community on the state of the business coming out of the critical month of May. We'll publish more details related to the date and time of the event a couple of weeks in advance.

With that, let's move on to today's call. As always, we expect to make forward-looking statements, so I want to caution everyone that our actual results could differ materially from what we say. Investors should familiarize themselves with the full range of risk factors that could impact our results, and those are filed in our Form 10-K, which is filed with the Securities and Exchange Commission. I also want to remind everyone that today's call is being recorded, and an archived version of the call will be published on our website.

With that, let's get started. And so I'll turn the call over to Jim Hagedorn. Jim?

James S. Hagedorn

CEO & Chairman of the Board

Thanks, Jim, and good morning, everyone. I'm only going to speak for a few minutes this morning. We shared a pretty comprehensive outlook during our Analyst Day meeting a few weeks ago, and I don't need to repeat the key themes you heard that day from the rest of the team.

Here's the main thing to take away from this morning's announcement and from this call: the business remains extremely strong, and our optimism about another great year continues to swell.

In our U.S. Consumer segment, retailers remain highly supportive and consumers are in full swing as we enter the peak weeks of the lawn and garden season. POS is up roughly 25% as we enter May, and we're seeing encouraging trends in recent weeks as we've begun to comp against last year's record results. At Hawthorne, we just posted our biggest 4-week sales month ever in April, continuing to build on the momentum we saw throughout our record first half and giving us the confidence to raise our sales guidance once again.

The innovation we talked about during Analyst Day continues to be a driving force for this business and is helping us put more distance between Hawthorne and the competition.

The only negative news we've seen has been related to issues beyond our control, and that's the cost environment. Just like about every other company that most of you are following, we continue to navigate

significant inflation in commodities. So I actually want to begin my remarks there and then transition to talk about each of the businesses for just a few minutes.

You'll hear from Cory that we're seeing more downward pressure on our margins than we expected. And as you saw in our press release, we're taking aggressive action to address it. Effective in the fourth quarter, we're implementing a mid- to high single-digit price increase in our U.S. Consumer business that will carry into fiscal 2022. We took a similar increase at Hawthorne.

Over the past 15 years or so, we've taken pricing in all but a few years. Usually, it's less than 100 basis points. That level of pricing has allowed us to continue to innovate. It's allowed us to invest in more marketing. It's allowed us to create a more technically proficient selling process at Hawthorne and to ensure we're nurturing our people at all levels and locations in the organization.

I don't like price increases at this level, I'll just say that. I'm not worried about elasticity in the Consumer business, and the price increase at Hawthorne has not had an impact on our order volume. But I'd prefer small and steady increases instead of a change like we're implementing this summer.

That said, every raw material we're buying right now is at a materially higher cost than we planned. Distribution costs are higher, too. So we're going to do what we need to protect the margin structure of the business in order to maintain the tools that we need to keep our business healthy and to behave like an industry leader should behave.

We're fortunate to be in 2 remarkably resilient categories. We're fortunate to have clearly differentiated businesses with real competitive advantages. So as long as we remain committed to delivering the value to people who use our products, I believe we'll be able to pass along these price increases with little to no disruption to our business.

With that, let's pivot and talk about our U.S. Consumer business because we continue to exceed our own expectations, which is giving us the potential for upside to the guidance we revised just a month ago. During our Analyst Day meeting, we moved our sales guidance for the U.S. Consumer business to a range of 4% to 6% after last year's 24% growth. However, it's already beginning to look as if that estimate was too conservative.

Right now, consumers are behaving almost exactly like they told us they would. Going into the season, 86% of consumers who entered the category last year told us they would be back. More importantly, 2/3 of them said they would gauge at an even higher level than they did last year.

The week after our Analyst Day event, we posted our first-ever \$200 million week of POS with our top 4 retail partners. On a full month basis, April POS was up about 25%, even when factoring in an extremely difficult comp in the last week of the month and the impact of a late blast of winter weather in the Midwest and Northeast that kept consumers in their homes the week prior.

As we saw last year, gardening activity continues to lead the way. Entering May, consumer purchases of our soils are up roughly 30%. Our lawn fertilizer business was up 15% year-to-date, and grass seed is up more than 35% entering May. This is the third straight year of double-digit growth in grass seed as we continue to benefit from the tremendous efforts of our lawns' R&D team. Control products are up approximately 20%.

Entering May, we remain up double digits in every region of the country with every major retailer. We continue to see a high level of engagement in all retail channels. Remember, though, May is a critical month for the business. We're up against a tough comp for the balance of the year, and we expect to give back some of our first half POS gains. But the level of consumer and retail engagement is better than we were expecting and is giving us confidence that we may have some additional upside volume on a full year basis.

Because so much of the year is still in front of us, we're not going to reset the sales number again this morning, but we will provide an update in early June. But as you know, we are resetting the Hawthorne numbers again this morning as that business simply continues to outperform all of our expectations. The second quarter marked the fifth straight in which Hawthorne reported at least 60% sales growth. The

business is now up 68% on a fiscal year-to-date basis. We continue to see strong growth in all Hawthorne categories, especially lighting in North America. Cory will cover the details in a few minutes. However, I do want to commend the team on the way they're operating the business right now.

Our commitment to innovation and our 360 selling process is manifesting itself as a distinct competitive advantage. We are not only driving growth, but continuing to distance ourselves from the competition and set the industry standard. While it is difficult to quantify market share in this space, we're confident we're outpacing our competitors. Hydro retailers see the clear advantage of working closely with Hawthorne, and commercial growers are continuing to see us as the clear leader in this space.

If you've not viewed the presentations we shared last month, I'd encourage you to go to our IR website and watch them. You'll quickly understand how and why this business is performing so well.

The growth at Hawthorne continues in all geographies. Our largest market, California, was up 80% in the quarter. Michigan rose 60%. And we saw triple-digit growth in 7 states, including Oklahoma, where the business grew 250% compared to last year's second quarter.

In addition to the current marketplace, since November, 8 more states, including 3 in the past 2 months, have either expanded their existing markets or allowed cannabis cultivation for the first time. Whether we see federal reform with this administration or not, clearly the momentum at the state level is not slowing down. We'll see more markets open and create more opportunities for growth. And I'm convinced we'll continue to spread our wings in the years ahead, building on our competitive advantages to drive growth and further solidify our leadership in this space.

Whether at Hawthorne or the U.S. Consumer business, we remain in a great place right now. The team is firing on all cylinders. All aspects of the business are strong. The M&A pipeline has lots of potential, and we have tremendous financial flexibility. I know I've been saying this for several years now, but I can't remember being this optimistic about our future. And I want our shareholders to know that we're not taking anything for granted. We see opportunity out there, but we know success won't simply fall into our lap. We've got to go out and capture it. I'm convinced we have the right team and the right strategy to do just that.

With that, let me turn it over to Cory to cover the financials.

Cory T. Miller

Senior VP & Interim CFO

Thanks, Jim, and hello, everyone. I joked during my Analyst Day remarks that I've had the good fortune of calling up our numbers nearly every time I've spoken publicly since I took on this new role. And here, I am again reporting on another strong quarter and once again in a position to update our guidance.

Obviously, the positive news this quarter continues to focus on the strong top line growth in both businesses. However, we're starting to see a bit more margin pressure than we expected. As Jim said, that will likely continue through Q3 and then begin to level out.

I'll get to the margin discussion in a bit, but let me start with sales in the quarter. Company-wide sales were up 32% in the quarter, and we were up 47% year-to-date. We said at the start of the year that we'd be ahead of our full year guidance at the halfway point, but this is exceeding those expectations.

The U.S. Consumer business was up 23% in the quarter and is up 39% year-to-date. We continued to benefit from retailers building inventory at the start of the season, though the overall growth rate in the quarter matched the percentage of year-over-year POS growth as well.

We normally don't spend time on the Other segment, which is primarily our Canadian business. However, that business was up 82% in the quarter and 75% year-to-date. So the growth in the quarter was worth more than \$40 million. The story in Canada is very much in line with the U.S. The consumer is highly engaged, and retailers are increasing their inventory levels to stay ahead of demand. It's worth noting that the profitability of the Other segment is up dramatically this year as well. We're not really investing much more in that business, so the upside is falling pretty cleanly to the bottom line.

Back to the U.S. segment. Jim said, we are seeing the potential for upside to our recently revised guidance after the strong numbers we posted in April. Retailers continue to aggressively place orders as they expect consumer demand to continue throughout the balance of the season.

Given the tough POS comps we have in May, we want to have more clarity before we make any adjustments to our guidance. That's obviously not the case with Hawthorne. We had a record sales month in March to close the quarter, which helped us post the 66% growth you saw in the press release.

During the quarter, U.S. lighting sales increased by more than 95%, and sales of growing environment products improved nearly 110%. Consumables were up strongly as well, led by more than 45% growth in growing media and 40% in nutrients.

The momentum carried into April, which was another record month, and gave us a strong start to Q3. That's what gives us the confidence to raise our Hawthorne guidance again to a range of 30% to 40% growth on a full year basis.

For the time being, we did not adjust our company-wide EPS guidance. We'll likely make another adjustment in June when we update you on the status of the U.S. Consumer segment. As Jim said, we're seeing more downward margin pressure than we expected, which is offsetting much of the upside we're getting from Hawthorne. In fact, the higher rate of growth on the lower-margin Hawthorne business is having more of an impact on our gross margin rate than we planned coming into the year. Company-wide gross margins on an adjusted basis were down 340 basis points in the quarter to 36.6%. On a year-to-date basis, the rate was 33.7% through March compared with 34.8% a year earlier.

While Hawthorne segment mix is a big factor in the decline, the biggest issue is commodity and distribution costs. This pressure is more than offsetting the considerable fixed cost leverage that has been a benefit of the higher volume we've been running through our supply chain. The pressure on gross margin rate is likely to continue in Q3, which is why we now expect the rate to decline 175 to 225 basis points on a full year basis.

As Jim said, we've already been aggressive with our pricing decisions in Hawthorne, and we'll take a significant price increase in our U.S. Consumer business as well. These increases should begin to help us later in the year and will obviously put us in a better position as we develop our business plans for fiscal '22.

It's worth noting that we entered fiscal '21 after negotiating a planned price increase in our U.S. Consumer segment to take effect in August and then run through fiscal '22. But as commodity prices continued to climb, we took an even more aggressive posture. As the industry leader in this category, we embraced the responsibility to continue to innovate and invest in marketing efforts to drive consumer engagement. It takes margin to make those investments. And our decision allows us to continue to invest in the business in a way that our retail partners would expect.

Let's move on to SG&A, which was up 18% in the quarter and 23% through the first 6 months. The increase is due to higher planned marketing and media costs as well as higher accruals for variable pay. The effect of variable pay in our P&L will begin to reverse in Q3, however, and when combined with lower stock-based compensation still should be a full year benefit of \$50 million or more.

I also want to note that we are not changing our SG&A guidance right now, which projects a year-over-year decline of 3% to 8%. However, as we begin to see potential upside in the U.S. Consumer business, we're likely to use some of that if it materializes as we expect to further invest in our brands. We would not look at those investments to pay off in the current year, but to help us continue to strengthen our relationship with consumers and drive the business in the future years as well. There's not a lot of news between SG&A and the bottom line. So I won't go through the rest of the P&L unless you want to cover it in Q&A.

Our non-GAAP adjusted earnings, which are the basis of our guidance and exclude restructuring, impairment and nonrecurring items were \$322.3 million or \$5.64 per share. This compares to \$253.8 million or \$4.50 per share a year earlier.

As I said, we're leaving our full year adjusted EPS guidance in place for now, which is a range of \$8.60 to \$9 per share. The high end of that range would mark more than a doubling of our earnings in just a 2-year time period.

Moving quickly to the balance sheet. We finished the quarter with a leverage ratio of 2.1x debt-to-EBITDA. As we told you last month, there are quite a few M&A opportunities in the pipeline right now, but we have more than enough capacity to make the investments we want while also increasing our CapEx and returning cash to shareholders.

Looking ahead, you may see us once again turn to the bond market to raise some capital and lock in long-term debt at the current rates. While this may have a short-term dilutive effect, we believe locking in money at these higher rates will be beneficial in the long run if you assume higher rates are on the horizon as we do.

Finally, you'll notice that CapEx is running behind the \$125 million to \$150 million investment that Jim and I discussed with you last month. Historically, the majority of our CapEx investment every year comes in the second half of the year, which we would expect to be true again this year. So that keeps us on track to deliver our revised guidance of approximately \$250 million in free cash flow, which we define as operating cash flow minus CapEx.

I'll close by saying I couldn't agree more with what Jim said a few moments ago. With the exception of commodity prices, which are beyond our control, the business is operating as well as I've seen during my 20-year tenure here. I'm extremely confident in our guidance. I see the opportunity to do even better and believe we're putting the company in a great position as we begin the planning process for fiscal 2022. So with that, I'll turn things back to the operator, and we'll open the call up for your questions.

Question and Answer

Operator

[Operator Instructions] We'll take our first question from Jon Andersen with William Blair.

Jon Robert Andersen

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

Congratulations. I wanted to ask -- start first about Hawthorne. I think Jim pointed out, this is the fifth consecutive quarter of growth above 60%. You taking your outlook up a couple of times now. And the growth has been exceeding what you've previously talked about as kind of a long-term expectation now for quite some time.

You also mentioned in the prepared comments the new states that have come online since November, which will probably go live in a more meaningful way over the next 12 to 18 months, which would seem to portend good things for Hawthorne over the next several years. So how are you thinking about the sustainable growth rate at Hawthorne over the next 2 to 3 years? And why couldn't we continue to see the kind of growth that you've been putting up more recently out of that business?

James S. Hagedorn

CEO & Chairman of the Board

Well, I do. Now just why you're talking -- like Cory's whispering 15%, something like that, which I think is a bunch of hooey. But remember, the one time I got crushed by you guys was when I said, I don't see why we couldn't sort of sustain 15% for a long time on this business, and then '18 happened. And then I think for those people who have followed us for a while, it was like the one thing I said if I made a mistake on, it's sort of committing to that kind of growth rates.

And so I agree with you, to be honest. I just think there's going to be a lot of resistance here to committing to a number that -- I try to remind everybody here that our push into live goods and Hawthorne was that these -- at the time, so go back 5 years, we looked at sort of our core North American Consumer business as a kind of 1% to 2% business and that we said we think we can pick up sort of 2 to 3x that growth rate at fair pricing with Hawthorne and live goods. And I think that's all been true.

The sustainability of the growth -- and this is my point of view, but -- so I'm really pleased looking at it, which is not due to any of my work, but due to the work that Chris and his team and Mike have put into actually building the business that we described to you guys a while with these really sort of -- these really serious competitive advantages, I think, that we're actually getting to the point -- and I think I asked this question of Chris couple of weeks ago: how far are we along in the path of creating the sort of -- where -- I hate the word, vendor, but if you say where we become kind of the perfect vendor, where we're actually good and a real value to our business partners. And I think you said about 80%.

So I think we still have ways to go. Supply chain, innovation, sort of technical selling, probably some additional product lines that we ought to be carrying. But I think if you look at the lighting business, which is a really good example of kind of bringing innovation to the business, I think that -- I don't want to throw a number out, but I think it exceeds what Cory would be comfortable with me saying.

I don't know if that answers the question. But I think we are building the business we should all be really proud of -- cory, go ahead. Cory wants to say something. Maybe we ought to ask Chris if he has a point of view.

Cory T. Miller

Senior VP & Interim CFO

Yes. And I'll just add on to that -- Jon, I'll add on to that, that during the month of April, we've transitioned 2 of our facilities into new larger buildings to increase our output, and we've opened a new

facility as well. So we see the growth going forward in the future. And we're trying to ramp up our supply chain to allow us to ship more product out than we have in the past.

As the prepared comments said, March was a great way to end the quarter, and April was a record quarter -- or a record month. So each time that we open a facility like this and allow our shipments out to increase, we're looking to have another record month going forward. So the growth is...

James S. Hagedorn

CEO & Chairman of the Board

Yes. But there's 2 ways to look at that. I think, Jon, we're on sort of generation 3 of sort of supply chain footprint as this business grows. And I think Mike would probably say, maybe that was a mistake. Generation 2 was a mistake, not thinking bigger because we're just sort of just settling down in a facility and finding out like that's not working. We need to do it again.

And I think -- it's a bit stressful. But I think we're leaving a lot of sales on the table. So we continue to, I think, on both businesses, to be honest. And a lot of credit goes to supply chain people for kind of keeping up. But I think if you said, are we a good vendor from a supply chain delivery on time in full? I don't know, Mike, what would you say?

Michael C. Lukemire

President & COO

I say we were getting better.

James S. Hagedorn

CEO & Chairman of the Board

But how would you grade us?

Michael C. Lukemire

President & COO

I'd probably give us a B minus.

James S. Hagedorn

CEO & Chairman of the Board

So I think that while it's true what Cory says, we open up a facility and we pick up sales, I think in part because we were leaving sales on the table when we couldn't deliver. So part of it is growth, and part of it is actually having a fulfillment system that is more successful at getting product out the door.

I don't know, Chris, anything you want to throw in?

Christopher J. Hagedorn

GM & Senior VP

Yes. Look, I think you guys have covered a lot of it. I do think Cory and Luke hit on -- our service levels, frankly, are not at a level that I'm personally satisfied with. I think we have some of our retailers on the call right now listening and I suspect, unfortunately, they'd probably agree.

Now we can still be better than our competition while not being as good as the standard we hold ourselves to. We're improving pretty rapidly and putting a lot of thought and effort and resources into improving that supply chain.

Like Jim, if I were able to give my sort of unfettered thoughts, I'd probably commit to a number that Cory would slap me for. So I'm going to hesitate from -- I'm not going to do that. But look, I'm extremely bullish about the outlook of the business. I think we're -- we continue to improve our service levels, which I think are our biggest bottleneck, frankly.

We've got some M&A in the pipeline that I'm extremely excited about that will fill some key product and portfolio brand gaps for us moving forward that we should be closing within this fiscal year.

So I'm really excited about this business. I think we can continue to improve it. And I think we've, to a large extent, been our own kind of worst enemy, and we're working hard to get around that. That's not to underestimate the strength and competitiveness of our competitors. But again, I think we've been standing in our own way, and we're working hard to get around that.

Jon Robert Andersen

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

That's super helpful. Just a quick follow-up on the pricing commentary. Have you priced already in Hawthorne? Is it at similar levels to what you described for U.S. Consumer, mid- to high single digit? And as the leader, do you expect competition to follow? Or have you seen them follow?

Christopher J. Hagedorn

GM & Senior VP

Yes, Jon. We've already taken our pricing. So it's been in market for about a month now. We haven't seen any impact on volume. On the contrary, it's been picking up. So we're saying, man, we should have taken more and we had the chance.

And this is one of the way -- areas we really like the breadth of our portfolio. It allows us to take pricing in kind of very precise areas and leave certain categories sort of untouched from a pricing perspective, and that's something that we think we can leverage much more than our competitors can.

As to do we expect competitors to follow suit, we do. Typically, what we've seen is it will be a month or 2 in lag from us that we'll see most of our major competitors follow suit very closely. So I don't believe we've seen that hit the market yet, but we're kind of just getting to the time frame where we'd expect it to be any day.

Operator

We're taking our next question from Bill Chappell with Truist Securities.

William Bates Chappell

Truist Securities, Inc., Research Division

I guess first question on the pricing and the timing of the pricing. I guess I think you had said for the U.S. Consumer business, it's going to happen more July, August and with the season largely done kind of by July 4. Just trying to understand, is it that you're already fully hedged for your -- most of your needs this year, and so you're just trying to take action for next year? Or will you see something sooner in terms of maybe lower promotions or something like that, that could impact May sales and June sales?

James S. Hagedorn

CEO & Chairman of the Board

I don't think you're seeing -- going to see lower promotions. I do think retailers are sensitive to margins right now, to be honest. I think they're seeing pricing all over the place for themselves. So -- but I don't think any action or anything we do, are going to result in any changes to promotion at the field on our product lines.

The increase in the summer is something that we've been talking about now for some months as we've seen the pressure sort of build. I think all retailers, I think, are aware of our actions that are headed their way.

I asked Mike to consider pulling forward the pricing. I think he didn't really want to do that. I understand why. It's a pretty big number relative to what people have seen historically in the past with us. It's kind of been a while that we've ever -- I think maybe one other time in my time here in that 20 years, have we looked at the sort of this level of pricing.

I don't think we have a choice here. I think Mike, when he's had discussions with the retailers, has said, we -- depending on what we see happening on commodities, we could have to go out again. But given, I

think, people's attitudes and I think the limited benefit to sort of take it now, I've become more relaxed with Mike's position of like I want to do it toward the end of the summer. And I'm okay with that.

In regard to hedging, I think we're pretty typical for where we've been for everybody who follows us on the hedging front. That doesn't mean we're not exposed, but I think we have largely been hedged. But it's still pretty eye-watering to see some of the increases that we're seeing.

And Mike, anything you want to add?

Michael C. Lukemire

President & COO

No. I think we had an agreement with retailers for August pricing, and we've taken the number up. And I think we chose to go that route. We're in pretty good shape on what we have left to produce. If you're seeing any pressure is that we -- in certain categories, we are overselling the plant like in soils that are causing -- you're buying at a higher level, so some of the higher costs are coming in a little bit earlier. So to me, that's the pressure that we're facing.

But we looked at the gap between May and August, and there wasn't just that much money we would net out with that. So we chose to stay with August.

James S. Hagedorn

CEO & Chairman of the Board

And I think another thing to add, just so people are clear, is we elected not to take any kind of significant pricing at all during kind of the COVID year, last year. And retailers were, I think, very much aware that we were taking a pretty benign position in regard to pricing last year as a result of not knowing what was happening and that, that was going to be a -- so part of this is catch-up as well.

Michael C. Lukemire

President & COO

Yes. Think about it as 2 years' worth of pricing here.

William Bates Chappell

Truist Securities, Inc., Research Division

Yes. No, no. And I understand that. I guess what I'm saying is so many of the CPG companies are taking pricing to get recovery in the second half. You're kind of taking it in your fiscal fourth quarter. So this is really more of a recovery for fiscal '22. Is that the right -- because I mean the prices that you're talking about today is not going to make much of a difference...

James S. Hagedorn

CEO & Chairman of the Board

Yes. The answer is yes.

Michael C. Lukemire

President & COO

Yes.

James S. Hagedorn

CEO & Chairman of the Board

It's simple. Look, again, I think maybe once, like right when I showed up and I was like, I think running Miracle-Gro at the time, so I was like a segment leader, we took pricing mid-season. But I think it's pretty disruptive in this business to take pricing in the season that -- and it just sets off pandemonium, a ton of resistance but the retail level to -- retailers to do that.

So I told Mike a couple of weeks ago, I think we should pull it forward. But I think they made good arguments to -- that a couple of months is not worth the trouble it's going to cause.

William Bates Chappell

Truist Securities, Inc., Research Division

Sure. And you're comfortable with your guidance without having to do it, which is great. My follow-up question, just on Hawthorne. Maybe a little different way to ask Jon Andersen's question of where is the growth coming from. I know on the lighting business, a lot of that was replacement lighting from existing customers. Some of that lighting business was just stuff that you couldn't even fill from last year. So just kind of a mix that you're seeing, is it from newer, more recent states, more recent customers? Or is it still being driven by just kind of replenishment of existing customers?

James S. Hagedorn

CEO & Chairman of the Board

Listen -- hold on. I'll start, Chris, if you don't mind. I really -- dude, you're a friend. And I'm not saying that as like some way to trick and come out. But I don't think that's right. I think if you look at the business now, I think 50% of the business in dollars is LED. So there's a major technical transformation occurring in this business that Gavita largely is benefiting from. It's gigantic.

So I think if you look at the business, clearly, there's more state room to play with. There are people converting. But I think there's a major innovation play here.

A lot of you guys may have known the sort of story. I think I've told you guys this that we work very closely with Michael Porter at the Harvard Business School. And Chris and his team, Mike Lukemire were all up there. And we were saying we're kind of assemble a bunch of stuff from other people's parts that we buy around the world. And we kind of follow technology that others -- this was the past, by the way.

And Mike went to use the lavatory, came back and everybody was looking stunned when he came back. And he said, "What happened here?" And Porter had said, "Dude, if you're just going to be followers, you have to sell that business because you'll probably get the most money you'll ever get for that business right now."

So I'm flying back at the end of the week with Christopher and he says, you're not going to -- I got to ask him how the Porter meeting go. And he said, but you're not going to like this. And that -- my reaction, I think, caused us to view lighting as a very important strategic platform for us in this industry.

And I am -- I think I've said this on the virtual investor meeting. I am so proud of the work they've done, where I think we've got the finest LED fixtures by far and a lot of innovation in the pipeline to really drive this business for a long time.

And so I think this is not just a matter of the market being a little bit bigger. And we had a bunch of orders we could fill and people are like -- old customers are buying some new lights. I think there's -- we have made so much progress as a strategic vendor and innovator in lighting that I think -- and anybody who wants to come visit with us as COVID winds down -- I'm saying you have an open invitation. We can meet here or we can meet in Oregon and kind of show you what we're doing, but it's impressive.

So Mike -- or Christopher, you deserve the one to answer this.

Christopher J. Hagedorn

GM & Senior VP

Yes. Look, I think you covered a lot of it. I do think there's a really good mix across the board of both replacement and new builds. I mean every new state coming online means a lot of new facilities for us, and so we're certainly outfitting those. We're seeing growth in places like Oklahoma that continues to really outpace our expectations.

In fact, this past month was the first one that Oklahoma had actually outpaced Michigan. So the growth is explosive there, and those are new builds. I want to say 100% but the vast of that majority.

Now places like California, look, new builds are still going up, but we've also -- we have designed our lights, particularly the LEDs, to be as easy a replacement product as possible. That's our new Gavita 1930 fixture is designed to be able to swap directly 1 for 1 in for an old HPS fixture.

That being said, we're still selling a heck of a lot of our or Gavita high-pressure sodium line that we continue to innovate on and make it a more cost-effective fixture, easier service, easier to manufacture, easier for our customers to mount. So we're really seeing growth across the board. It's hard to peg it in one particular area.

Cory T. Miller

Senior VP & Interim CFO

Yes. And I'd just add on that LEDs are about 50% of our lighting business. And if you think of our total North America business, LEDs are about 15%.

Operator

The next question comes from Joe Altobello with Raymond James.

Joseph Nicholas Altobello

Raymond James & Associates, Inc., Research Division

Just had a couple of questions. First on margins. Are you guys pricing to offset the cost increase on a dollar-for-dollar basis? Or do you expect to maintain your margin structure as we head into fiscal '21 -- '22, sorry?

Cory T. Miller

Senior VP & Interim CFO

We're looking to price to make sure we're maintaining our margin structure. And if you look at our margins today, we've seen a little decline in margin. Some of that's related to the segment mix as Hawthorne, being a lower-margin business, grows faster than the U.S. Consumer business. The enterprise-wide margin declines a little bit. But within each of the businesses, we're trying to price to maintain that business's margin structure.

Joseph Nicholas Altobello

Raymond James & Associates, Inc., Research Division

Okay. And so if I interpret your answer here correctly, given the hedges that you have in place and the pricing that's coming in August, we're probably unlikely to see the gross margin outlook for '21 drift lower from here, it sounds like?

Cory T. Miller

Senior VP & Interim CFO

The plan is right now, given where commodities are and where we think they're heading, that our margins will be in a very similar ballpark to where we are this year. We'll continue to go through the plan and see if there's additional pressure based on continued cost increases. But right now, we're looking to kind of maintain the structure that we have.

Joseph Nicholas Altobello

Raymond James & Associates, Inc., Research Division

Okay. Great. And just if I could shift gears a little bit to the U.S. Consumer. I know we're still very much in 2021, but how are you guys thinking about that business for next year? I know you think the business is a 2% to 4% grower over the longer term. But do you anticipate that business might take a step back next year after what appears to be 2 very strong years in 2020 and 2021?

Michael C. Lukemire

President & COO

Well, I would never say go backwards. So I think we're going to learn a lot here in the -- in May and June. And so -- but the conversations I've had with retailers, they're bullish even about 2022. So they're getting in earlier. They're staying longer. And we plan -- and this is part of where we want marketing activities to continue to bring consumers in.

So I would say I would expect to be above 0. I'm not going to put a number out there yet because they're all looking at me so...

James S. Hagedorn

CEO & Chairman of the Board

Well, I think people get nauseated if they put a negative in there. But I think on the -- that virtual conference we did, I think we implied that there could be a retrenchment next year. So I wouldn't be surprised by that.

So I think that Mike doesn't want to say we have no evidence to show that would be true, but I think we're trying to be responsible. And so Joe, you know how to take that, I think.

Joseph Nicholas Altobello

Raymond James & Associates, Inc., Research Division

So Mike is more aggressive than Jim at this point, it sounds like?

James S. Hagedorn

CEO & Chairman of the Board

I think, look, Luke has -- look, for the last 2 years, the most accurate predictor of the business has been Mike Lukemire. I think Randy said that a bunch of times is that when he believed he couldn't trust his own finance team to forecast properly, he'd tell Mike, "What do you think?" And then he'd come back to me and say, "I think Mike was the most accurate sort of barometer out there."

I think Mike tends to be gung ho and optimistic. I've spent a lot of time trying to talk him down recently just from a safety point of view just because -- we've got like kind of cool wet weather here at the beginning of May. And I'm looking at my sort of wall clock that says it's the 5th of May. It feels like we haven't had crappy weather for like 1.5 years. It seems that way to me.

So I'm just -- I'm trying to keep Mike -- there's no negatives in here, by the way. What I mean by that is our numbers are still conservative enough that we're talking to you guys about that I don't really see an outcome that we don't meet or exceed what we're telling you guys.

So -- and what we are getting from this weather is the ability to sort of reset our supply chain, get our back in stock. And I think we've talked about this before, our people are tired. And so I think a little bit of weather now actually lightened things up. And as long as I can keep Luke's positiveness controlled, I think we end up with harder sort of angular changes. In the fighter pilot business, square corners are always a pain in the a**. They hurt.

So I think that what we're seeing right now and Mike's attitude actually feels pretty good to me at the moment. And so -- but he's pretty positive. And we'll just see what next year -- and what I've told Mike is, look, this next investor conference that you guys go to, where we sort of talk about the results through June -- or through the beginning of June, is a really important date for us as we look at our manufacturing forecasts and our outlooks for the year. But it's not scary from your guys' point of view. It's more how far do we overrun? Because I think what Luke is inputting right now is actually bringing the numbers up, not down. And I'm trying to just kind of moderate that a little bit, mostly looking at inventory at year-end.

Michael C. Lukemire

President & COO

But how the consumer takeaway in the back half of the year will affect '22. And that's what -- and then we'll know more. So if it's strong, I think it's really positive. If it slows down, then we could look at what happens in '22 to start the season.

Operator

We're taking our next question from Eric Bosshard with Cleveland Research.

James S. Hagedorn

CEO & Chairman of the Board

Eric, you there?

Eric Bosshard

Cleveland Research Company

Sorry, I'm here. Yes, I'm here. I'm sorry about that. A couple of things. First of all, in terms of clarity on your comment on gross margin for next year, I just wanted to understand, is the '22 gross margin assumed in line with '21? Or is 22% assumed to recover what was given up in '21, again, ex the segment mix? Which is the outcome we should be thinking about for '22 at this point?

Cory T. Miller

Senior VP & Interim CFO

We're currently looking at '22 to be in line with our current expectations for '21.

Eric Bosshard

Cleveland Research Company

And so there's not a recovery -- there's no point of recovery of the giveback in '21? Is that right?

Cory T. Miller

Senior VP & Interim CFO

We look at the recovery to come over potentially a 2-year period. As we look at what's happening with commodities, the pricing that we have in place, the balance of those 2 items are going to kind of drive the amount of recovery that we can have in '22.

Eric Bosshard

Cleveland Research Company

Okay. That's helpful. And then secondly...

James S. Hagedorn

CEO & Chairman of the Board

Hold on. Let's just throw it in there, Luke.

Michael C. Lukemire

President & COO

Yes. No, assuming the mix is the same.

Cory T. Miller

Senior VP & Interim CFO

That's right. From a segment mix -- assuming the segment mix is the same.

Michael C. Lukemire

President & COO

That's where it gets difficult. If you're looking across the total company, Hawthorne's growth. And then are we looking to recover those margins by segment? Yes. Is the mix different for the overall company? That may vary. That's what I think he's talking about.

Cory T. Miller

Senior VP & Interim CFO

Yes. Does that make sense, Eric? Or do you want me to dig into that a little bit more?

Eric Bosshard

Cleveland Research Company

Yes. No, I understand what you're saying. Secondly, I appreciate the transparency of nobody knows for sure what the numbers will look like in May and June. Your guidance implies the May and June POS down in the 10% kind of range. Is that the -- am I doing the math right to just level set what the guidance implies in terms of those months?

Cory T. Miller

Senior VP & Interim CFO

Yes. Our current guidance would say that full year is kind of mid-single digits, and the upcoming months are kind of flattish.

Eric Bosshard

Cleveland Research Company

Okay. And then the last question, the better-than-expected Hawthorne -- and I know that you want to answer both. I'd love if you didn't. But the upside in California and the upside in new markets, is it -- which one is most notably different or better than your expectation, the established markets or the new markets?

Christopher J. Hagedorn

GM & Senior VP

Well, I'll answer first. This is Chris. And if Cory or Jim or Luke want to elaborate there, obviously, welcome to. I think to me, the bigger surprise -- look, new markets, we expect to be to be pretty explosive for us. The continued performance out of California is more of a pleasant surprise to me. We see really good continued growth out of that business, both existing kind of legacy consumers and cultivators and newer commercial guys. It's been a really pleasant surprise for us. So I'd say that has been more of a standout than the new markets, in my opinion.

Eric Bosshard

Cleveland Research Company

And Chris, why do you think that's happening?

Christopher J. Hagedorn

GM & Senior VP

I think it's continued pretty explosive growth out of the, again, what we refer to as legacy cultivators. I think that's a lot of what's driving it as well as just the rollout in the recreational market is still, I'd say, probably not in its infancy, but it's probably in its kind of adolescent years. The recreational market in California has not yet reached a state of maturity like I think you see in a place like Colorado. So you can -- we're just continuing to see really, really strong growth from those larger commercial accounts as well as just all the retail activity in California that services primarily those legacy growers.

James S. Hagedorn

CEO & Chairman of the Board

I just want to throw out, just to make my team here uncomfortable, Eric, I think we still meet our Street numbers even if we have double-digit declines sort of -- kind of for the rest of the year. Is that correct? I think that's correct. So I think what you said is pretty much correct.

No, I don't think we see it that bad, by the way. Not at all. So therefore, we continue to be positive just because the hurdles for the rest of the year are not that high.

Eric Bosshard

Cleveland Research Company

Okay. That's helpful.

James S. Hagedorn

CEO & Chairman of the Board

And I agree with what Chris said, by the way. Just that if you look at -- just hold on there, operator, the legacy states, California, Michigan, sort of our big states, just the performance in those real established states, #1 and #2, just continued to be really positive and drive a lot of business.

James D. King

Chief Communications Officer & Executive VP

Let's go ahead and with the Q&A.

Operator

We're taking our next question from William Reuter with Bank of America.

William Michael Reuter

BofA Securities, Research Division

With regard to your comments around lots of M&A and then another comment about potentially going back to the high-yield markets, I guess what would be the size that you're looking at? I assume that this is all going to be on the Hawthorne side. And then, I guess, what would be the multiples that you're seeing at this point for those types of businesses?

James S. Hagedorn

CEO & Chairman of the Board

I think most of what we're looking at is on the Hawthorne side, but we continue to be interested in live goods as well. Multiples, I think, are probably slightly higher on the Hawthorne side than they have been. We continue to be determined not to overpay. And I think historical multiples on the sort of consumer side are sort of in that 8-ish range.

I think that -- so I would say the mix probably favors, at least in deal -- kind of unit volume, favors Hawthorne. Although I think we continue and have been outspoken of our desire to sort of continue to solidify and strengthen the Bonnie business.

William Michael Reuter

BofA Securities, Research Division

That's helpful. And then just with regard to size, how large are the M&A opportunities that are out there, either in terms of sales, EBITDA, something like that? Just to give us a little bit of a sense. And that's all for me.

James S. Hagedorn

CEO & Chairman of the Board

More money than we could spend. I think it's a very interesting time. It was, I think, key thematic with -- as we went through that virtual Investor Day is that the opportunities to further build this business with volume is probably as robust as I've ever seen it. And therefore, I think we have quite a bit of choice, and we've been kind of clear with folks on that, which is that there's enough opportunity out there and we don't have unlimited capacity that we have choice to choose. And in many areas, we have multiple choices for kind of a given segment. And therefore, we can sort of afford to hold our ground on value.

So size, I think core Hawthorne, these aren't huge deals. Live goods, you could spend more money. But they're just a lot bigger, so 500-plus, something like that.

Operator

We're taking our next question from Carla Casella from JPMorgan.

Unknown Analyst

I'm calling in on behalf of Carla. I know you guys alluded to it a few other times earlier how much the gross margin pressure will be offset by price hikes. What we wanted to ask was if you guys had any sort of early read on the potential acceptance level of these price hikes? Or are you seeing any volume pullback as perhaps [indiscernible] in this quarter?

James S. Hagedorn

CEO & Chairman of the Board

I'll let Mike -- because Mike somewhat has to sort of put these to bed. But I'll start with the simple thing from my point of view. It's not negotiable, okay? If you look at sort of where this money is being consumed -- you know my point of view. And I think you guys -- anybody is -- it's a nonending front page of the journal kind of pressure on people who manufacture and buying raw materials.

We took effectively nothing last year. And if you look and said, how much of that money is being spent, it's probably 3/4 of it already. So -- and I don't think we're really saying anything different from other vendors in sort of, call it, DIY hardware. Remember, the pricing has gone in already at Hawthorne and was accepted without any sort of pressure on orders.

The retail environment is a bit different on the consumer side of the business. So I hope we don't get threatened because I just -- I don't see any value in that. We're not -- this is not some greedy thing. This is just looking at what we're paying for. And so it's really not negotiable.

I don't suspect we're going to get any kind of significant pushback. I mean, verbal, we probably will and have, but I think that interferes with the business. I think it's -- the probability of that is low but not 0.

Mike, you're the one that's responsible for doing it.

Michael C. Lukemire

President & COO

No. I mean this is probably the first time we have to actually do this. And so we'll work with the retailers on the program. And if commodities were to go up again, we've already indicated that it could be higher. So we're trying to get it and work together and solve the problem together and not get into a volume game. This is a lot different than historic negotiations. This is real issue for all of us, and they're facing those issues as well. So -- but we'll get it resolved. And so I think the discussions are good at this point.

Operator

We take our next question from Alex Maroccia from Berenberg.

Alexander Rocco Maroccia

Joh. Berenberg, Gossler & Co. KG, Research Division

The first one is on Hawthorne and new markets. It sounds like New York learned a lot from the tough rollout in California in how they're going to tax. So I mean it could be a bit more successful from the start than the California market was. However, this market won't come online until Q4 '22. So do you think there's a scenario in early calendar '22 where Hawthorne growth looks a bit light on the tough comps and then you see a spike later in the year? I guess, generally, I'm just trying to figure out how material new markets have been for the business in the past few quarters.

Cory T. Miller

Senior VP & Interim CFO

Yes. As we look at the individual states that have come online, new markets like New York are much, much smaller. It's -- California is like 100x the size of New York, just to put it in perspective. So as the rollout happens, there could be some bumps in the road on how that rolls out, but it's on a very, very small base. So it's something that won't even be noticed in our results.

But after everything gets in place and we start operating kind of on the new way in a legal state, we expect continued increase in the percentage growth to be really, really strong in those new markets. But we don't see the pain of getting to that growth like we did in California in 2018 because we just don't have a large established market there already. So it's going to roll out in a different way than those earlier states just because of the size.

James S. Hagedorn

CEO & Chairman of the Board

Chris, anything you'd add there?

Christopher J. Hagedorn

GM & Senior VP

No. I think Cory covered it. Look, New York is going to be a monster market for us, but it will take a little time for that to develop. So I don't think we'll see lightness there. I think the growth in New York is incremental upside for us.

James S. Hagedorn

CEO & Chairman of the Board

It kind of goes back to that first question, which is what do you think the sustained growth rate is going to be for Hawthorne. And that's sort of when you define light, I think goes to what number. I don't think you're ever going to hear us say assume a 60% growth rate. Cory kind of whispered across the table, tell them 15%. Tell them -- and Chris and I said, we -- it's hard for us to even say that.

But remember, we have gotten burned. So it sort of depends on where you are there. But I think that if you just look long term, which is what I would hope you guys can do, is if you look at Pennsylvania, New Jersey, which is a red state, New York's now a red state, say they come online kind of fully over a couple of year period, dude, that's like California on the East Coast, and that's got to be good.

And so I think that's how we're looking at it. But I do think it's -- what is the growth rate that you guys are willing to commit to on Hawthorne. Or maybe I should put it this way, what are you guys going to input into your models that we can sort of react to because I think we're likely to be sort of on the low end, not because that's what we're seeing, just because we got burned pretty hard when I said I think 15% a year is a good number. And then like, I think, within 2 years -- I felt like, seriously, like it was the biggest mistake I've made with you guys in a long time, is committing to a growth rate that -- I think looking back on now, you'd say, dude, that was a good safe number. But for like 1.5 years, it felt like one of the largest mistakes I ever made as far as speaking too quickly. I think that was at an investor conference down in Florida.

Michael C. Lukemire

President & COO

We only look forward now. Don't look back.

James S. Hagedorn

CEO & Chairman of the Board

No. I do look back on that one. So I think if you look long term and you say we're growing the business, creating a sort of essential partner to cultivators. So if you see basically the map getting bigger, the strategy of Hawthorne getting sharper, implementing the sort of essential tools that make us a real partner to our cultivator partners, plus dealing with margin rate issues, which -- margin on Hawthorne is quite a bit better than it has been. And therefore, while it's lower than our corporate average, there's been significant improvement.

It's just hard if you'll put all that stuff together to say anything other than long term, Hawthorne has been, from our point of view, a lot of fun. And I think our Board is -- we just met, but I think the Board is very respectful of kind of the strategy that we developed around entering this business and been very supportive and so has the whole management team.

And so that if you just -- again, we introduced, I think, people to you guys. But if you look at the strength of the management team on sort of the big 3 parts of the business or maybe 4 parts, but that is the Consumer business, the Hawthorne business and then the Scotts underlying foundation, dude, it's a pretty cool business and I think worth investing in.

Alexander Rocco Maroccia

Joh. Berenberg, Gossler & Co. KG, Research Division

Okay. That's all helpful. Got it. And then second one is on M&A based on one of the previous questions. Where do the synergies lie with layering on businesses to Bonnie? And would these be Bonnie-like businesses, just in different geographies?

James S. Hagedorn

CEO & Chairman of the Board

Look, I'll start by saying Bonnie -- yes, I guess, Bonnie-like. But I don't think there is a good proxy for Bonnie. Bonnie has a really unique business, and it starts with the brand. There's a lot of plants out there. But what Bonnie owns is they -- is a branded business with a very sort of unique distribution and service model that I think is -- and I don't think anybody has that.

So I think while Bonnie is not the largest business in the sort of green space, I think it's the most valuable and the most unique and suits us well. So I think things that we're looking at, we'd want to be able to include there -- and look, if you look at -- Mike knows these numbers better than I do. But if you say we've got a couple of thousand people in-season in stores, Bonnie has probably got 1,000, something like that.

Michael C. Lukemire

President & COO

1,500.

James S. Hagedorn

CEO & Chairman of the Board

People in stores. Everybody is putting people in stores. And what did we learn from Scotts North America, which was taking all these businesses and putting them together back in the day is that nobody wants like 4 salespeople, 4 invoices, 4 trucks, forklifts, all the trouble that goes with that. So I'm really focusing on synergies here.

The ability for us to -- and it's been a kind of a dream of mine. I don't know if it's a great idea still, okay? But it has been a dream of mine to be able to say in a Depot or Lowes, could we have a full-time team that never is on the road driving around store to store. It deals with just our stuff partnering with store management. And I think if we look -- and so again, read synergy here. The ability for us to be able to do that, I think, is getting closer and closer. Mike?

Michael C. Lukemire

President & COO

Yes. No, I agree. And I think you think about the effectiveness of the space in the stores and how you make it more effective and not fighting over space. But the store growth with less space means you've got to be more effective. And we think the live goods solution can actually help in those areas.

James S. Hagedorn

CEO & Chairman of the Board

And I'll throw out that -- I'm not going to show you we're the only one that can do that, but I think we're one of the only ones that actually has the horsepower, starting with Bonnie, to be able to offer that kind of -- and it's because it's -- well, there may be synergies in dollars, I think there are on our side. Just think about the synergy of effectiveness of in-store operations. The -- this was King, I'm sure is going to want me to shut up here.

Let me tell you, this is one where because we do our own thing in stores and you see a lot of other vendors, marketing people like us who have bought into buying into the retailer programs, I'll tell you one thing you're seeing this year, is an incredible lack of ability to get labor, okay? We're set, but I think retailers are having a tremendous issue. And the competitive advantage of having the -- which I call just the footprint in store, the amount of concrete we own in the store, to be able to put our own army in there and you say we can extend that into other parts of the business, I think it's very powerful and offers a gigantic like benefit to the retailer that -- I think if any of you guys talk to retailers, they would say Scotts is in a very small group of vendor partners who can put the kind of power into the store. It's maybe us and Behr Paint. I don't know that anybody else is, particularly non-lumber, can do that kind of work that we do. And so I think the execution benefit to the retailers is gigantor.

Operator

It appears there are no further questions at this time. Mr. King, I'd like to turn the call back to you for any additional or closing remarks.

James D. King

Chief Communications Officer & Executive VP

All right. Thanks, Anita. Thanks, everybody, for joining us this morning. If you've got follow-up questions or want to talk about things we didn't get a chance to address, again, just call me directly at (937) 578-5622. And as I said, at the outset, Cory and I will be updating our status of the business in early June at the William Blair Conference. We'll issue a press release a couple of weeks out on the details of that conference, and more likely than not, be issuing a press release associated with the comments that we make at that event.

So otherwise, we'll hang up at this point. Thanks for joining us today, and have a great spring, everybody.

James S. Hagedorn

CEO & Chairman of the Board

See you guys.

Operator

This concludes today's call. Thank you for your participation. You may now disconnect.

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