

14-Sep-2021

Core & Main, Inc. (CNM)

Q2 2021 Earnings Call

CORPORATE PARTICIPANTS

Robyn Bradbury

Vice President-Investor Relations, Financial Planning & Analysis, Core & Main, Inc.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

OTHER PARTICIPANTS

David John Manthey

Analyst, Robert W. Baird & Co., Inc.

Jamie Cook

Analyst, Credit Suisse Securities (USA) LLC

Keith Hughes

Analyst, Truist Securities, Inc.

Joe Ritchie

Analyst, Goldman Sachs & Co. LLC

Matthew Bouley

Analyst, Barclays Capital, Inc.

Kathryn Ingram Thompson

Analyst, Thompson Research Group LLC

Anthony James Pettinari

Analyst, Citigroup Global Markets, Inc.

Nigel Coe

Analyst, Wolfe Research LLC

Mike Dahl

Analyst, RBC Capital Markets LLC

MANAGEMENT DISCUSSION SECTION

Operator: Hello and welcome to the Core & Main Q2 2021 Earnings Call. My name is Charlie and I will be coordinating your call today. [Operator Instructions] I will now hand you over to your host Robyn Bradbury from Core & Main to begin. Robyn, please go ahead.

Robyn Bradbury

Vice President-Investor Relations, Financial Planning & Analysis, Core & Main, Inc.

Thank you. Good morning and welcome to the Core & Main fiscal 2021 second quarter earnings call. This is Robyn Bradbury, Vice President of Investor Relations and FP&A for Core & Main. Thank you for joining us this morning to attend our first earnings call as a public company. We're thrilled to share our results with you.

Steve LeClair, our Chief Executive Officer, will lead today's call with the company overview and our second quarter execution highlights. Mark Witkowski, our Chief Financial Officer, will then discuss our second quarter financial results and second half outlook, followed by a Q&A. We will conclude the call with Steve's closing remarks. For Q&A, please limit to one question and one follow up. If you have additional questions, you may return to the queue. Thank you for your cooperation.

Some of the information you will hear today may include forward-looking statements. They may include statements regarding our intentions, belief, assumptions, or current expectations, concerning our financial position, results of operations, cash flow, prospects, or growth strategies. Forward-looking statements are subject to known and unknown risks and uncertainties, many of which may be outside of our control. We caution you that forward-looking statements are not guarantees of future performance or outcomes and that they may differ materially from those made and/or suggested by the forward-looking statements contained on this call. These forward-looking statements are made only as of the date of this call. We do not undertake any obligation to update or revise any forward-looking or cautionary statements to reflect changes in assumptions, the occurrence of events, or changes in the future operating results.

In addition to providing results that are determined in accordance with US GAAP, we present EBITDA, adjusted EBITDA, adjusted EBITDA margin, adjusted net income, and net debt leverage, all of which are non-GAAP financial measures. These measures are not considered measures of financial performance or liquidity under GAAP, but we use them to assess the operating results of our business. For a reconciliation to the nearest GAAP measure, please refer to the slides in the appendix of the fiscal 2021 second quarter investor presentation, which can be found on our Investor Relations website.

Thank you for participating on the call and for your interest in Core & Main, I will now turn the call over to Chief Executive Officer, Steve LeClair.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Thank you, Rob, and good morning, everyone. Thank you for joining us today and welcome to our fiscal 2021 second quarter earnings call, our first earnings call as a publicly traded company. This is an exciting milestone for our company and I am very pleased to be sharing it with you. I'll begin today's call with a brief overview of our business and industry. I will then cover our key growth drivers and acquisition strategy, followed by a review of our ESG characteristics. I will end by discussing our second quarter execution highlights before turning the call

over to our Chief Financial Officer, Mark Witkowski to discuss our fiscal 2021 second quarter financial results and second half outlook.

I'll start on page 5 of the presentation with a brief overview of Core & Main. Core & Main is a leading specialty distributor of water, wastewater, storm drainage, and fire protection products and related services, serving municipalities, private water companies, and professional contractors across municipal, non-residential and residential end markets nationwide. Our specialty products and services are used in the maintenance, repair, replacement and construction of water and fire protection infrastructure. We are one of only two national distributors operating across large and highly fragmented markets, which we estimate to be approximately \$27 billion in size.

With more than 285 branches across the US, we serve as a critical link between over 4,500 suppliers and a diverse and long-standing base of over 60,000 customers. We have diversified end-market exposure with an estimated 45% municipal, 37% non-residential and 18% residential end-market mix in fiscal year 2020. Furthermore, we had near equal exposure to construction on new projects and existing repair-and-replace projects in fiscal year 2020.

On page 6, we provide an overview of our broad product offering and service offering. We offer a comprehensive portfolio of over 200,000 SKUs, covering a full spectrum of specialized products. At the core of our business are the pipes, valves and fittings, which are the fundamental building blocks for underground water infrastructure and water treatment plants. Above ground and in many types of structures, you will see our fire protection line. Fire protection infrastructure requires not only a specialized set of products, including sprinklers and valves, but also the ability to fabricate and assemble sprinkler systems and their components.

We are national distributor of smart water meters, which bring significant environmental and economic benefits to municipalities and also provide a variety of value-added services, including not only project management, installation, hardware and software, but also life-long meter system management. We are also a national provider of storm drainage and geo synthetics and erosion control solutions, which are growing in importance due to the recent impacts of climate change and increased natural flooding disasters.

On page 7, we show the strong value proposition we offer to both our customers and our suppliers. We are a trusted source to our customers because of our operational excellence across a broad offering of products and services. We take a consultative sales approach, leveraging our deep understanding of local specifications to help design material project plans and offer key value-added services throughout the life of the project.

Our role as a national distributor is more than just supplying products. We have access to a broad product offering and have the ability to secure products for any job and in any environment for our customers. Paired with our national branch network, we also offer complementary value-added services that are key to our value proposition, which we believe differentiate us from our competitors. We have longstanding relationships with our suppliers and in many cases, we benefit from favorable purchasing arrangements and preferred or exclusive access to products, especially during periods of material shortages.

Our geographic footprint and reach to local communities is essential to our suppliers, because we have a highly developed understanding of the market, the customer base, and the growth opportunities. We believe we have the ability and expertise to drive the adoption of new products and technologies and offer the logistics of last-mile delivery and customer support. We have a large and highly trained sales force with the ability to reach our highly fragmented customer base.

On page 8, we outline the levers that enable us to drive sustainable growth. Over the past few years, we have invested in people and capabilities to strengthen our ability to drive growth. As we look ahead, we see multiple avenues to continue pursuing. First, we see beneficial industry trends supported by secular growth drivers. The traditionally stable municipal landmark is poised to accelerate as additional spending is necessary to address historical underinvestment and support population growth.

Residential construction is currently surging due to population growth, demographic population shifts, low housing inventory, and record-low interest rates. With the surge in residential construction comes a long tail of rejuvenated non-residential investment, as communities expand and demand increases for our waterworks, storm drainage, and fire protection products. We believe we're at the beginning of a new non-residential construction cycle and see favorable tailwinds ahead, particularly in verticals such as commercial and institutional buildings, data centers, and warehousing development projects.

We have several organic growth levers. We have demonstrated that we can grow faster than our underlying addressable market. We believe our competitive advantages allow us to continue to gain share at the local level. With only 14% share across an estimated \$27 billion addressable market, we still have significant opportunity to grow. We continue to drive organic expansion to under-penetrated geographies through new greenfield locations. We have meaningful runway to increase penetration with strategic accounts. We have a specialized team focused on serving strategic accounts, which include large private water companies and national contractors.

We believe we are better positioned than ever to serve these national customers on larger projects requiring dedicated sales personnel, greater technical expertise, and more complex or specialized procurement needs. Our size and scale positions us to continue accelerating the adoption of products in our industry such as smart meters, fusible HDPE technology, geosynthetics, and erosion control solutions and number of other developing product categories.

Acquisition is another key component of our growth strategy. We have a long runway to consolidate our fragmented industry. Our focus includes consolidation of existing market positions, new geographies, and expansion into product categories where we are clearly under-penetrated. I'll discuss our acquisition strategy in more detail in the coming slides.

Finally, we have identified a long list of opportunities to enhance gross margins, including private label through global sourcing and pricing and procurement initiatives. As of fiscal year 2020, private label made up roughly 1% of our total product expenditures. We believe that we have an opportunity to transition several hundred million dollars' worth of ancillary spend to be internally sourced, but we have no intention of transitioning highly specified products into private label or disrupting any products from our top-tier supplier partners.

We have recently built a team of pricing analysts who have been able to enhance product margins using data to drive pricing decisions and by proactively updating price increases to increase pricing visibility to our branch network. Additionally, our category management team has opportunities to continue shifting spend to suppliers with the best pricing and payment programs in order to optimize gross margins. We are in the early innings of executing on many of these initiatives and see a long runway of opportunity ahead.

On page 9, we provide a timeline of our recent acquisitions. We have a strong track record of acquiring and integrating businesses, and we continue to cultivate a robust pipeline of targets for the short and long term. We have executed and integrated 14 acquisition since becoming an independent company in 2017, adding more than \$630 million in aggregate historical annual net sales, including two recent deals that closed subsequent to the second quarter, which I will discuss in more detail shortly.

We have a refined process of identifying attractive bolt-on targets and we are well-positioned to source, acquire and integrate new businesses. We believe we are widely viewed as the acquirer of choice due to our longstanding relationships and entrepreneurial culture, and our investment in the development of our people. We seek to generate margin improvement and synergy value from our acquisitions through purchasing capabilities, fixed cost reduction and the use of our scalable IP platforms, which drive operational efficiencies at our branches.

Our industry is large and highly fragmented. As we look ahead, we see a runway for growth through M&A. We maintain a very robust pipeline of future acquisitions, which we pursue through our disciplined approach. We prioritize complementary businesses that help us consolidate existing market positions and expand into new geographic areas, acquire key talent and offer new products.

On page 10, we show our newest acquisitions, L & M Bag & Supply and Pacific Pipe. The Pacific Pipe acquisition highlights our focus on expanding into under-served geographies. Pacific Pipe a significant player in modernizing and expanding water infrastructure in Hawaii, a state we had no presence in previously. Pacific Pipe has been in operation since 2011, serving municipalities and contractors in the water, wastewater, storm drainage, in the irrigation industries, with a broad waterworks product offering. Pacific Pipe operates four locations spanning the islands of Hawaii, Maui and Oahu.

The L & M Bag & Supply acquisitions highlight our focus on expanding our presence in under-penetrated product categories. It provides a sizable growth opportunity in the large and fragmented geosynthetics and erosion control market, which we estimate to be roughly \$5 billion in size. Over the past three decades, L & M has built itself into one of the nation's leading suppliers of geosynthetics and erosion control products. By joining our team together, we will expand our expertise to better serve our customers nationwide, have a larger reach for our products and services, with a dedicated team of specialists serving the rapidly growing and highly specialized geosynthetics and erosion control market.

Annual net sales of Pacific Pipe and L & M Bag & Supply for the fiscal year ended December 31, 2020, were roughly \$70 million and \$60 million, respectively. And both acquisitions will be incremental to our sales and earnings growth for the majority of the second half of fiscal 2021.

Turning the page 11, we share our ESG characteristics. ESG is core to our business model. Our company and our people are committed to the provision of safe and sustainable water infrastructure throughout the United States. Preserving the Earth's most valuable resource and providing clean and safe water to our communities, are the core of what we do. Our products and services are integral to building, repairing, and maintaining essential water, wastewater, storm drainage, and fire protection systems. Water is a finite resource and community water supply challenges, including natural flooding, contamination, and drought, continue to increase in severity.

We partner with our customers to help ensure water resources and facilities are available to meet each local communities' short- and long-term needs. We believe our investment in our people, [ph] for out (00:14:49) award-winning training and career development, is a true differentiator for us. We are proud we have seasoned experts who are preparing the industry leaders for tomorrow, to continue our tradition of local experts nationwide. We are deeply committed to our communities and our associates.

Our inaugural ESG report that was published last fall, has become a critical piece of communication with all of our stakeholders. We believe that our focus on ESG matters, and sustainability will benefit our business by enhancing our relationships with our associates, our customers, our suppliers, and the communities in which we operate. We will continue to focus on this area and enhance our communication reporting around ESG over time.

With that, I will now cover our second quarter execution highlights on page 12 of the presentation. During and subsequent to the second quarter, we successfully completed our initial public offering of approximately 40 million shares of Class A common stock, generating gross proceeds of approximately \$800 million, including the full exercise of the underwriters' over-allotment option. We used the proceeds from the offering to deleverage the balance sheet, positioning us with greater financial flexibility to pursue our growth strategies.

While the IPO is a great milestone for us, we remain focused on driving solid business results in a very dynamic environment. In the second quarter, we delivered record net sales of nearly \$1.3 billion, growing nearly 36% over the prior-year period and record adjusted EBITDA of \$155 million, which was nearly 57% over the prior-year period. We continued to expand our market share and improve our profitability through the execution of our sales and margin initiatives, while using our leadership position in the industry to gain access to hard-to-find products for our customers and purchase opportunistically ahead of announced product cost increases to expand our gross margins.

Earlier this year, PVC resin manufacturers declared force majeure due to raw material shortages stemming from plant closures as a result of unprecedented winter weather in Texas and Louisiana. It was the second force majeure on PVC resin in less than six months and the ripple effects were felt across the entire supply chain. Industry-wide PVC manufacturing capacity and inventories declined, while demand strengthened which pushed PVC pipe prices to an all-time high. In recent months, PVC pipe manufacturing returned to full capacity and our PVC suppliers have been working to rebuild inventory. Demand has continued to be strong and prices rose through the second quarter. The impact of Hurricane Ida is still not fully known, but we expect that it will likely further impact availability of PVC products and keep prices at or above those we have experienced so far this year.

On a smaller scale, but growing in significance, we are also experiencing supply chain impacts in other product categories due to unprecedented demand, constrained manufacturing capacity, container shortages, port issues, and semiconductor chip shortages. A portion of our smart metering products have chip components that are in short supply and that has impacted our ability to satisfy all the customer demand. Some of our suppliers import raw materials or finished products, and we're beginning to see an impact to the cost and supply of those products, due to the declining availability and rising costs of import shipping containers. We are also seeing some deferral of shipments as a result of constrained labor capacity across the industry, from our suppliers to our customers.

Despite these notable challenges, our teams have navigated the environment well. Given our long-term relationships with our suppliers and our leadership in the industry, we are often able to gain preferred access to products during periods of material shortages and provide reliable service to our customers nationwide. Through coordinated efforts with our branches and leadership team, we believe we have gained market share by successfully mitigating the impacts of these supply chain events by ensuring access to products and providing advance notice of cost increases and reliable information on product availability to our customers.

I'm incredibly proud of the dedication of our customers and suppliers during this challenging environment. More than ever, we have served as logistics experts for our customers, helping them find and source products during a period of unprecedented pricing increases and product shortages, while providing credible market information to our suppliers regarding demand, to assist them with production planning. As previously mentioned, we continue to execute on our growth strategy by announcing two new acquisitions during the quarter, L & M Bag & Supply and Pacific Pipe Company, both of which closed subsequent to the quarter.

We continue to closely monitor the impacts of COVID-19 and the variants that have surfaced across the country. Throughout the pandemic, we continued to operate as an essential business, providing our customers with the products and services necessary to maintain and improve our nation's water infrastructure. At the beginning of the pandemic, we put policies and business continuity plans in place to protect our associates, customers, and suppliers. Our teams have remained agile and have quickly adapted to new protocols while increasing efficiency throughout the process. As vaccine rolled out en masse and as cities began loosening restrictions, we also began easing certain COVID-19 protocols, while still keeping safety our number one priority. We are committed to keeping our associates, customers, and suppliers safe, while continuing to keep all of our branches open.

Subsequent to the end of the quarter, the Senate passed the bipartisan \$1 trillion INVEST in America Act, the largest long-term federal investment in our nation's infrastructure in nearly a century. Among other things, the plan makes transformational and historic investments in clean water infrastructure, an infrastructure that provides resilience to the changing climate.

While it's still uncertain if or when the bill will be signed into law and when the funds will start making their way into our end markets, a direct infusion of federal funds for water, wastewater, and storm drainage infrastructure, has immense implications to accelerate repair and replacement activity. We believe we are well-positioned to capitalize on any favorable tailwinds created by the additional investment. However, we are well-positioned to continue to grow even without this potential infusion of funds.

I will now turn the call over to our Chief Financial Officer, Mark Witkowski, to discuss our fiscal 2021 second quarter financial results and second half outlook.

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

Thank you, Steve. Good morning, everyone. Turning the page 14. And I'll begin by covering our second quarter operating results. Net sales in the second quarter were nearly \$1.3 billion, an increase of approximately 36% over the prior-year period. The increase was driven by volume gains and higher average selling prices relative to the prior-year period.

Our sales benefited from demand across each of our end markets. Residential and construction has continued to benefit from strong housing demand and [ph] lap (00:22:06) development. The municipal end market has started to see an acceleration of growth. Our non-residential end market which contains a mix of project types ranging from commercial buildings to roads and bridges, saw varying results but overall experienced positive [indiscernible] (00:22:22) growth in the quarter.

Our execution of sales initiatives and our leadership position in our industry has allowed us to outperform our end markets and deliver solid core share gains, by ensuring our customers have access to the products where and when they needed them. We believe roughly half of our net sales increase for the quarter was due to price inflation, which was much higher than expected and driven by our team's ability to efficiently pass through rising material costs. We experienced rapidly rising material costs on PVC pipe, in addition to many other product lines but to a lesser extent than PVC. Our teams have done a fantastic job navigating the inflationary environment and working closely with our customers to give them advance notice of these market price increases.

Pipe valves and fittings sales increased nearly 43% compared to the prior-year period, due to a mix of strong volume gains and price inflation from rising material costs. The same factors drove growth in our storm drainage and fire protection product lines, which were up 21% and 37%, respectively, compared with the prior-year period.

Our metering product line grew by 9% compared with the prior-year period. Metering growth was tempered by the global semiconductor chip shortage, which is a necessary component in certain smart metering devices.

Gross profit in the second quarter increased 41% to \$325 million. Gross profit as a percentage of sales was 25.1% compared with 24.1% in the prior-year period, an improvement of approximately 100 basis points. The increase in gross profit percentage was primarily due to improvements in product sourcing and pricing.

Given our scale, we've been able to make opportunistic inventory purchases ahead of announced price increases, which has helped slow the growth of the net cost of our products during an inflationary period. We believe our initiatives to get better visibility to these cost increases from our vendors to our field teams has resulted in gross margin enhancement. We also continue to make progress on our private label initiative and double the amount of internally-sourced products relative to the same quarter last year.

Selling, general and administrative expenses for the second quarter increased 40% to \$192 million. The increase was primarily attributable to an increase in personnel expenses, driven by higher variable incentive compensation, resulting from higher sales volume and stronger profitability. In addition, we experienced higher head count and discretionary expenses due to furloughs and spending reductions in the response to COVID-19 in the prior-year period. SG&A expenses also increased by \$17 million related to higher equity-based compensation expense, due to accounting for equity awards and \$1.3 million related to costs associated with the initial public offering.

As a result of our debt refinancing, we recognized a net loss on debt modification and extinguishment during the quarter of \$50.4 million. This amount consisted of early redemption premiums, deferred financing fee write-offs, settlement of our cash flow interest rate swap instrument and non-capitalized third-party fees. Annual interest expense savings as a result of the debt refinancing is expected to be roughly \$85 million.

Adjusted EBITDA grew 57% to \$155 million, improving adjusted EBITDA margin by approximately 160 basis points. The increase in adjusted EBITDA margin was due to strong net sales growth, gross margin rate expansion, and leveraging our fixed cost structure on the sales growth. Adjusted net income increased 215% to \$61 million. The increase was due to strong sales growth in gross margin rate expansion, partially offset by higher SG&A expenses, primarily attributable to higher variable compensation cost during the period.

In preparing adjusted net income, we exclude the effects of non-controlling interest as we evaluate and manage the business as a whole. For a reconciliation of net income to adjusted net income, refer to the slides in the appendix of the presentation.

On page 15, I'll now cover our debt and liquidity position at the end of the quarter. Our net debt at the end of the quarter was \$1.433 billion, bringing our net debt leverage down to 3.3 times, which is 1.9 turns favorable to the prior quarter. The reduction in net debt leverage is primarily a result of net proceeds generated from the initial public offering, the refinancing transactions taken in connection with the IPO and an increase in adjusted EBITDA. We expect to continue deleveraging the balance sheet, similar to what we have accomplished in the past, despite making strategic investments to grow the business which may include acquisitions.

We closed down the refinancing of our new \$1.5 billion term loan in conjunction with the closing of our IPO, which carries interest at LIBOR plus margin of 250 basis points, maturing in July 2028. We correspondingly entered into a five-year fixed interest rate hedge with an initial notional value of \$1 billion to lock in LIBOR rate at 74 basis points. The notional value will reduce by \$100 million per year beginning in July 2023 through the end of the hedge term.

As part of the debt refinancing, we also expanded and extended our asset-based revolving credit facility from \$700 million to \$850 million through July 2026. At the end of the second quarter, we had over \$900 million in liquidity, including approximately \$67 million of cash and cash equivalents. We believe that our cash on hand, together with the availability of borrowings under our asset-based revolving credit facility and cash generated from operations, will be sufficient in the near-term to meet our working capital needs, anticipated capital expenditures, scheduled principal and interest payments on our term loan and to continue pursuing our growth strategies.

Operating cash flow in the second quarter was less than the prior-year period due to the acceleration of interest payments associated with the debt refinancing, along with investments in working capital to support our growth. We have continued to invest in inventory to ensure availability and access to products for our customers. These investments along with the growth in the business compared to last year, resulted in a larger working capital build in the current quarter. Historically, we have generated most of our operating cash in the second half of the year as we unwind working capital with the reduced inventory spending and lower customer receivables. We expect to see a similar seasonal generation of operating cash flow in the second half of this year.

Subsequent to the end of the quarter, the underwriters of our initial public offering exercised their over-allotment option, which resulted in the issuance of an additional 5.2 million class A shares, generating net proceeds of \$99.5 million. We intend to use the net proceeds for general corporate purposes.

Turning to page 16, I'll now discuss our outlook for the remainder of fiscal year. We expect the demand and pricing trends we experienced in the first half of the year to continue into the second half, though tempered against tougher prior-year comps and anticipated supply chain constraints. Last year, we experienced a softer first half due to COVID-19-related restrictions and a snapback in demand in the second half as cities loosened restrictions and markets began to recover, as well as favorable weather environment in the fourth quarter. Each of our end markets appears poised for continued growth based on bidding activity and order flow. And the execution of our defined growth initiatives is expected to continue, driving core market share gains.

While we are pleased with our results so far this year, we believe that our supply chain is experiencing capacity constraints across many product lines, which we anticipate will be further impacted by Hurricane Ida. We believe this will temper volume growth in the second half of the year, while keeping prices at historically high levels through the end of the year. We typically experience a seasonal slowdown throughout the second half of the year and the fourth quarter in particular, is susceptible to variability due to cold winter weather in northern geographies.

The Pacific Pipe and L & M Bag & Supply acquisitions will contribute nearly half a year of operating results each, with Pacific Pipe closing at the beginning of August and L & M Supply closing at the end of August. On a combined basis, these acquisitions generated roughly \$130 million of net sales for the fiscal year ended December 31, 2020.

We maintain a very strong pipeline of high-quality acquisition targets and look forward to adding more of them to the Core & Main family. Our acquisitions are performing well and we continue to improve our ability to integrate them into our company and create synergies together.

We expect to continue delivering on our gross margin initiatives, generating year-over-year margin expansion in the second half though moderated compared to the first half as our product costs catch up with market prices if product costs stabilize.

We also expect to continue leveraging our cost structure, delivering year-over-year SG&A rate improvement in the second half. However, the SG&A rate improvement will be scaled compared to what we delivered in the first half

as a result of approximately \$10 million of ongoing annual cost needed to support our company following the initial public offering.

Taken all together, we expect full-year 2021 adjusted EBITDA to be in the range of \$470 million to \$510 million, representing a year-over-year increase of 37% to 49%. There are several uncertainties that exist for the balance of the year that could significantly impact our estimates and position us towards the lower or higher end of the range. The ongoing COVID-19 pandemic, product availability constraints, labor shortages, declining commodity prices, and unfavorable weather, could position us towards the lower end of the range. Sustained pricing levels and gross margins, continued demand across each of our end markets, along with our suppliers' ability to meet demand, could result in performance near the top end of the range. Given the unprecedented pricing, demand, and product availability challenges we're experiencing right now, we feel that this range represents our best view of where we believe we'll finish the year.

I'll now cover a few topics of interest unrelated to our second quarter performance, regarding our organizational structure and tax receivable agreements. In terms of our share structure, we currently have roughly 246 million shares of Class A common stock and Class B common stock issued and outstanding. Shares of Class A common stock and Class B common stock have the same one-for-one voting rights. Class B shareholders do not hold economic interests in Core & Main, Inc. However, they have the ability to exchange one share of Class B common stock and one partnership interest in Core & Main Holdings LP for one share of Class A common stock.

The Class B shareholders ownership of partnership interest in Core & Main Holdings LP is reflected on our consolidated financial statements as non-controlling interests. Over time, as these exchanges take place, the non-controlling interest will reduce in size. In evaluating and managing the business as a whole, we exclude the effects of non-controlling interests. As part of our IPO, we reorganized the company is an Up-C structure, which enables us to retain certain favorable tax attributes and potentially generate sizable new favorable tax attributes. In an Up-C organization, it is typical to enter into tax receivable agreements with the pre-IPO owners to establish the terms of how the favorable tax attributes will be shared. A summary of the details of each TRA is located in the appendix of the presentation.

Assuming the full exchange of Class B shareholders of their shares of Class B common stock and partnership interest to shares of Class A common stock at the closing stock price per share of Class A common stock as of July 30, 2021 and current tax rates, we anticipate a substantial reduction in our cash tax rate. Net of the payment obligations under the TRA, we expect this net cash savings to be in the low- to mid-single-digits of pre-tax book income. Further, TRA payments are not made unless tax benefits are actually realized. I hope you find this additional detail helpful as we introduce our business and our structure.

In closing, we are very pleased with our second quarter performance and first half results. We continue to focus our efforts on increasing market share, improving profitability, and generating consistent operating cash flow. That concludes our prepared remarks.

At this time, I'd like to turn the call over to the operator for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question is from David Manthey of Baird your line is open. Please go ahead.

David John Manthey

Analyst, Robert W. Baird & Co., Inc.

Thank you, good morning, everyone. Of the...

Q

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Good morning, Dave.

A

David John Manthey

Analyst, Robert W. Baird & Co., Inc.

...43% growth. Yeah. Of the 43% growth that you saw in PVC, can you approximately quantify the impact of inflation versus volume growth? And I think, you had previously been assuming that the PVC will start to decline in the second half, are you now assuming that will be sustained into 2022 at current price levels?

Q

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

Yeah, Dave, I'll answer on the pricing for the quarter and PVC. I'd tell you a little – [indiscernible] (00:37:12) certainly over a half of PVC was going to be pricing. Obviously, we had a bigger impact on PVC than some of the other product categories. So, the kind of the best target I can give you on PVC in terms of the impact there. In terms of the go forward, Steve, you want to talk about that?

A

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Yeah. Dave, [indiscernible] (00:37:31) certainly PVC has been disrupted significantly over the last year from Hurricane Laura last fall to the deep freeze that happened in Texas in the beginning of this year, to now Hurricane Ida. So, we are seeing demand at all-time highs and product availability and supply at all-time lows. So, given those dynamics, we feel like we're going to see that pricing hold in there through the duration here at least for the next several months.

A

And so, along those lines that was – we obviously didn't expect to see pricing carry through as strong as we had this year. We expect it to taper down to more stabilized levels. But given some of these external factors, we think it'll probably hold in there for a bit.

David John Manthey

Analyst, Robert W. Baird & Co., Inc.

Okay. Thanks. And as it relates to the \$55 billion in the current infrastructure bill, if that goes through and if those dollars start to filter down to the municipalities, might there be some crowding out relative to already stretched municipal budgets or do you think that's all incremental?

Q

And then, second, if you can just comment on just the debate around infrastructure, do you view that as a positive long term that maybe there's changing attitudes, changing priorities in the US as it relates to infrastructure spending today at any level?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Yeah. Dave, I would say that even if you go back to the back half of 2019, we started seeing municipal in infrastructure spend starting to really grow and accelerate. Obviously, it took a pause in second, third quarter of 2020 due to COVID, but it's continued to be – remained very strong, demand has remained strong. I think, the municipalities are certainly better positioned now. They've been able to get rate unlike they've been able to do a decade ago. So, along those lines we feel those budgets are really strong and secure.

Now, obviously, if you throw in an infrastructure bill and \$55 billion dedicated to modernizing, clean drinking water systems across America, we do think that's all incremental based on what we're seeing. Now, if and when that bill gets passed and how those funds get down there, we'll see how that plays out. I do think the industry is much better positioned than when we were a decade ago with infrastructure spending in that sector.

David John Manthey

Analyst, Robert W. Baird & Co., Inc.

Q

It sounds great. Thanks, very much, guys.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Thanks, Dave.

Operator: Our next question comes from Jamie Cook of Credit Suisse. Your line is open, please go ahead.

Jamie Cook

Analyst, Credit Suisse Securities (USA) LLC

Q

Hi, good morning. Nice quarter. I guess, just two questions. Sorry to harp on the PVC pipe again, but your margins in this quarter were really impressive. Your gross margins, I think, [indiscernible] (00:40:28) which might be a record for you guys. I'm just wondering, was a lot of that PVC pipe and can we – can margins sort of sustain in that level in the back half? I'm just trying to think about how we get to your increased EBITDA guidance? And then can you help us understand what the EBITDA contribution is from the two acquisitions in the back half? Thanks.

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

A

Yeah. Thanks, Jamie. Thanks for the question. In terms of PVC and the gross margin impacts, we really saw nice margin improvement across really all of our product lines. As I mentioned, we did see some material cost increases across the board. Certainly, larger on PVC, but we were able to manage those pretty well across the board. And in the case of PVC that was no different.

So, we've realized some margin improvement there. As those prices start to increase, we're able to buy PVC pretty well during the environment and get those passed along at the appropriate timeframe, which is certainly much better than we've been able to do in the past when we've seen rapidly rising material increases. So, I'd say,

it's really across the board where we were able to pick up some margin enhancement across various product lines.

Jamie Cook

Analyst, Credit Suisse Securities (USA) LLC

Sorry. Again, gross margins sustained in that – at the 25% range in the back half and then just the EBITDA contribution from the two acquisitions in the back half was implied?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Yeah. I think, Jamie, that the way that we're looking at the back half in terms of margins is still being able to sustain those. But I would say as these prices stabilize, we would expect the cost side of the equation to catch up and see a little of margin compression there. Typically, were a little stronger in the back half anyway. But that's kind of how to think about the back half. In terms of the EBITDA increment for the acquisitions, I would tell you that post synergy we expect both of those to be accretive to the business.

Jamie Cook

Analyst, Credit Suisse Securities (USA) LLC

Okay. Thank you.

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

Yeah. Thanks.

Operator: Our next question comes from Keith Hughes of Truist. Your line is open, please go ahead.

Keith Hughes

Analyst, Truist Securities, Inc.

Thank you. Question on the effects of Ida. I know you said it was still to kind of be figured out, but do you have – do you know how the timeframe or what your suppliers are telling you in terms of when they'll know what the situation looks like? Is this within a week, or is this going to drag on for months?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Yeah. A tough question, Keith, as we look at it. So, certainly, when you look at the impact, [ph] and it was that (00:43:18) the biggest impact we've seen obviously is PVC. So, during that time period, when Ida came through, it's kind of shuttered about 40% of the PVC capacity in Louisiana and Texas. So that's one challenge is getting those plants back up and running, power being restored. And then the second challenge, which is a little bit more unpredictable, is going to be the transportation situation, particularly rail and truck in and out of there.

So, we anticipated somewhere in the neighborhood of four to six weeks, somewhere in that ballpark, where we're going to be seeing the after effects of that. It could be longer, it could be shorter. But we do expect somewhere in that ballpark. And it's kind of day-by-day right now as we go through it.

Secondary impact to Ida has really been, at a much lesser degree, has been the weather impact that it's had across the country. When we get into areas that have been inundated with wet weather, often times our

contractors were unable to dig into saturated soil. So, that can push things out a week. But that's to a much lesser extent and certainly something that we're used to when we get into weather events like that. But the PVC piece is going to be one we're going to have to be sorting out over the next several weeks.

Keith Hughes

Analyst, Truist Securities, Inc.

Q

Okay. And just along the same lines, are you able to do any substitution with the customers with ductile iron or HDPE, or anything to kind of bridge the gap or is that – that is too much?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Yeah. We've certainly seen situations where either due to price or availability, there have been material substitutes at levels we haven't quite frankly have seen before in the past. I would share with you also that even with ductile iron pipe availability that a premium as well too, as manufacturers are really at capacity at this point. The inventory in the network is at all-time lows as well too. So, it's going to be a challenge working through all of those product categories to find viable substitutes.

Keith Hughes

Analyst, Truist Securities, Inc.

Q

Okay. Thank you.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

But I would say that the good news is and this really does play to our strengths on this, Keith, and that one of the things that we really prided ourselves and one of our differentiators is access to product and being able to support customers through this. And then, secondarily, as where appropriate, finding substitutes for those products and pulling that through. So, more so than ever, our customers are leaning on us pretty heavily for that.

Keith Hughes

Analyst, Truist Securities, Inc.

Q

Okay. Thank you.

Operator: Our next question is from [ph] Pat Bowman (00:45:53) of JPMorgan. Your line is open, please go ahead. [ph] Pat (00:46:05), your line is...

Q

I'm sorry. I think, I was – yeah.

Operator: Go ahead.

Q

I think, I was on mute, I'm sorry about that. Good morning, everyone. Can you frame for us in the quarter relative to that 18% volume growth, how each of the end markets trended relative to that? I'd assume resi was above that and maybe – I don't know, I'll let you answer that.

And then, as a follow up to that, can you give a sense on expectations for second half volume growth across those end markets, like which ones are being most impacted by supply constraints? Just curious if you could flesh that out a little bit more? Thanks.

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

Yeah. [ph] Pat, (00:46:43) thanks for the question. Good morning. Yeah. For the quarter, I would tell you, right, resi certainly the strongest of the end markets, I'd say, well into double digit category there. And then, non-resi and muni, certainly nice growth in the quarter. I'd say, muni typically than our – stronger than our typical kind of low-single digit, we did see some nice strength in muni. And then, non-resi kind of in that same range. So, really good performance across those. I'd say, going into the back half, everything we see right now is fairly consistent across those end markets with continued demand and tailwinds. No real impact due to product availability that would impact any end market more than the other.

Okay. And relative to kind of the volume versus price growth in the second half, like how would you frame kind of – it sounds like you'll get more price growth than volume growth? So I just wondered if you could flesh that out a bit as well on the revenue side?

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

Yeah. I think, it will look a lot like the first half of the year with the exception being the fourth quarter where we started to see pricing pick up last year due to the effects of the hurricanes last fall. That's when we really started to see some of the initial price increases come through in PVC. So, you'll see price be a little less of a story most likely in the fourth quarter relative to the – at least the second and third quarters.

Okay. And then, my follow-up is on the M&A pipeline. Can you guys just update us on the size of the pipeline and then kind of your opportunity to execute on that given the current balance sheet leverage post these recent deals that you've executed on?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Yeah. Thanks. We've got a really strong pipeline, continue to really find opportunities out there. So, if you look at the deals that we just closed subsequent, it was really good indicators of what we've been able to do with bolt-on acquisitions in new geographies and then new product enhancement. So, our pipeline continues to be robust. I think, in the short and medium term, you'll see probably deals in a smaller range of the \$5 million to \$30 million revenue over the next few quarters. But we continue to see a lot of opportunity out there. Certainly, the tax situation and the potential legislation that's being contemplated has really stirred a lot of interest and a lot of potential sellers as well too. So, we continue to be encouraged by what we're seeing with that pipeline.

From a capital structure, really no impact whatsoever with going public, so we continue to have ample liquidity to pursue all of our M&A targets, in addition to just great cash flow characteristics where the business really well positioned to continue the M&A pipeline.

Q

Great. Thanks for the color. Best of luck.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Thank you.

A

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

Thanks, [ph] Pat (00:49:54).

A

Operator: Our next question is from Joe Ritchie of Goldman Sachs. Your line is open, please go ahead.

Joe Ritchie

Analyst, Goldman Sachs & Co. LLC

Thanks. Good morning, everybody.

Q

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Hey. Good morning, Joe.

A

Joe Ritchie

Analyst, Goldman Sachs & Co. LLC

So, my first question is really just around pricing for 2022. So, clearly a lot of pricing going through this year. I'm just curious how does – how does that look then potentially for 2022, you give back a little bit to your customers on price if we start to see commodity prices kind of stabilize? And then also, I'm just curious on how to think about the gross margin implications as well?

Q

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Yeah. Joe, really it's difficult to assess what's going to happen in 2022. Certainly, what we've seen is pricing has remained firm, we – a little better than expected. Certainly, we saw in second quarter and then we anticipate that to carry through in the short-term. But as for 2022, we'll just have to wait and see how this plays out. There's so many different dynamics in play right now in terms of demand and capacity constraints and everything else. So, it's really hard to give color on that at this point.

A

Joe Ritchie

Analyst, Goldman Sachs & Co. LLC

Q

Okay. No. That's fair. I guess maybe just maybe one follow on to that though. I mean, I guess Steve would you expect there to be some stickiness to price depending on what happens with commodities, if commodities were to let's say, flatten from here? Or is there typically some type of – if you're getting double-digit pricing this year, I don't know, you've got to give back like half of that next year? I'm just trying to figure out if there's a [ph] heuristic (00:51:35) around it?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Yeah. Typically, we do see some stickiness to that. So, the pricing will -while costs may deflate a little, the pricing in the market does tend to be a little bit more sticky over several months and so that's pretty traditional of what we've seen. So, there definitely would be a lag on there in terms of when the deflation starts hitting.

Joe Ritchie

Analyst, Goldman Sachs & Co. LLC

Q

Got it. That makes sense. And maybe my one follow-on on free cash flow, you clearly – you're building a little bit of working capital this year just given the environment that we're in. Again, I know it's probably really difficult to answer for 2022, but at some point if the supply chain environment again kind of stabilizes, should we get some type of working capital relief from your business?

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

A

Yeah. Joe that's something we'll obviously be watching really closely here, especially as we get through to the end of the year. You'll certainly see a release just due to our typical kind of seasonal line down or to some extent in the northern geography. So, we would typically release a little working capital. But as you look forward and beyond, we're going to have to watch the supply constraints very closely and make some decisions about when and where we make those investments.

Joe Ritchie

Analyst, Goldman Sachs & Co. LLC

Q

Got it. That makes sense. Thanks, everybody, and congrats.

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

A

Sure. Thanks, Joe.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Thanks, Joe.

Operator: Our next question is from Matthew Bouley of Barclays. Your line is open. Please go ahead.

Matthew Bouley

Analyst, Barclays Capital, Inc.

Q

Good morning, everyone. Thanks for taking the questions. First one on the gross margin side, you talked about some of that opportunistic pre-buying I guess ahead of the price increases. And I think at the same time I heard you say that in the second half, you expect costs to more so catch up. So, my question is, is there any reason

why we wouldn't see a kind of similar pre-buy benefit in the second half, given some of these more near-term inflationary trends, kind of how do you balance those two together? Thank you.

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

A

Hey, Matt, thanks for the question. I think, as we look into the second half, it's really about product availability and what happens to those pricing levels, so sustained pricing. So, pricing kind of, I'd say, stabilizes and flattens, we would expect that cost side to catch up a little and see probably a little pressure there in the second half. If they continue to rise like they've been, we'll continue to take advantage of those buying opportunities. And I think, we get a little benefit out of that in the back half. So, that – some of those challenges are what is driving kind of the range that we gave for the second half is just really seeing what ultimately happens on availability and price in the second half.

Matthew Bouley

Analyst, Barclays Capital, Inc.

Q

Understood. Okay. Very helpful there. And then, second one on the non-residential end market. I think, you made a comment at the top, you sounded relatively confident kind of being, I think, you said the beginning of a non-res cycle. I'm just curious what you've seen in your own business in terms of whether it's backlog or quoting in certain verticals, actually seeing a tangible uptick yet or you're making sort of a longer-term call based on some of the longer-term indicators you're seeing? Thank you.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Yeah. We look at non-residential really in two ways. So, there's certainly roads and bridges which has been storm drainage, which has continued to be very strong. And then for commercial construction, which really, our fire protection products are obviously instrumental in a lot of commercial construction. That was an area that was hit pretty hard during COVID. And what we're starting to see and we didn't anticipate, a big resurgence this year, but we're already starting to see a lot of quoting activity. We're already starting to see that area firm up.

We've been doing a lot of warehousing and data center work for fire protection systems and that's continued to carry through. And we're actually now starting to see a lot more commercial construction in some of these markets that were really challenged during COVID. So that's encouraging to us. We think that has some really good tailwinds ahead of us and the start of a new cycle.

Matthew Bouley

Analyst, Barclays Capital, Inc.

Q

All right. Well, thank you, Steve and thank you, Mark.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Thanks, Matt.

Operator: Our next question is from Kathryn Thompson of Thompson Research Group. Your line is open, please go ahead.

Kathryn Ingram Thompson

Analyst, Thompson Research Group LLC

Q

Hi. Thank you for taking my questions today. There has been some focus on the headwinds from weather events like Ida, Hurricane Ida, but what are the opportunities and how do weather events like these highlight Core & Main solutions, particularly around climate change and other disruptive weather events? Thank you.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Yeah. Thanks, Kathryn. Yeah, one of the things that we're seeing is the climate change situations have really emanated with some bigger large scale projects that are out there that may not be as visible to everybody. But we look at water source projects where there's been drought areas, you look at projects like in Lake Mead, for example, we've been very active in a number of these big treatment plant and water source projects. Same thing in the Wisconsin and some of these areas that are really struggling in a lot of ways to be able to find new water source. The strategic account teams that we have that work with the lot of the large national contractors and engineering firms have really enhanced our business and the ability to pull through those products. And what they like about [indiscernible] (00:57:36) is the ability to work at a national level and then have the local expertise and fulfillment capability. So that's giving us a real advantage.

We'll continue to see that too with a lot of the flooding situations, as more infrastructure investment goes into storm drainage and water retention systems and things along those lines. We're right at the forefront of that. We work with a lot of our vendor partners and helping to establish specs for new detention and retention systems for more efficient commercial construction and prevent water run-off into streams and other waterways. So, those things are all really playing into some of the strengths that we built as a business and particularly with these strategic accounts and then couple that with our local presence, it's given us a big advantage to continue to be able to support those needs as climate change has more impact.

Kathryn Ingram Thompson

Analyst, Thompson Research Group LLC

Q

Okay. Thank you. And then the – my follow-on question. You provided a lot of detail today on supply chain, how you're managing it, everything from meters to PVC have been impacted. But against this backdrop, you're not alone from a distribution standpoint and managing supply chain. What if any ways have you been able to determine if you're gaining market share given your size, your specialty nature and your national footprint?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Yeah, Kathryn, there's no doubt that given our size and scale, we're able to get preferred access to a lot of products that are really in short supply right now. And I just shared there a lot of our smaller competitors unfortunately don't have that ability to be able to do that. And we've been able to pick up quite a bit of business associated with that. Secondly, is when there are big material shortages like this, working on the consulting way in which we do with our sales process, we work diligently to try and find if we can't get the product, whether the alternative types of materials that can be used in this to complete these projects. And that's a big part of the value that we provide there and understanding a lot of the local specifications and being able to provide them solutions to how to complete these projects.

If you look at our – we've talked a little bit about labor shortages, our contractors right now have pretty significant labor challenges as well too. So, when they have a crew, they do not want that crew sitting idle waiting on materials. And so that's an opportunity where we can really help them in so many different ways and being able to

either get access to that product or find alternative material choices for them to complete those projects and keep their workforce active.

Kathryn Ingram Thompson

Analyst, Thompson Research Group LLC

Q

Okay. And then, just one final follow up just on your guidance which was better than expectations. What has been relatively better or – and what has been relatively worse versus your expectations as you were planning for this fiscal year?

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

A

Yeah, Kathryn. Thanks, for the question. I would tell you as we were planning for the year initially, certainly the rapid increase and the continued increase in product pricing that we've seen from our suppliers is certainly at levels that we had never seen and that we certainly didn't anticipate. One thing we were able to do, again and I think was more unique to this year than what we've done in the past, was the ability to get that pricing into the hands of our field teams faster. And we were able to see a nice gross margin improvement through this rapidly inflationary environment. So, I'd say, both of those items while we were preparing for this environment and ready for it, certainly, we executed I think better than we could have even anticipated through that. So, those are two of the big areas.

And then, obviously, the strength in demand coming out of COVID as well. While we saw some nice increases and tailwinds coming, certainly, it's been nice to see for our industry. So, those are all areas really combined to the – ultimately where we're at here with the full year guidance.

Kathryn Ingram Thompson

Analyst, Thompson Research Group LLC

Q

Perfect. Thank you, very much.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

And thanks, Kathryn.

Operator: Our next question is from Anthony Pettinari of Citi. Your line is open, please go ahead.

Anthony James Pettinari

Analyst, Citigroup Global Markets, Inc.

Q

Good morning. With the availability issues that we've...

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Good morning, Anthony.

Anthony James Pettinari

Analyst, Citigroup Global Markets, Inc.

Q

Hey. Good morning. With the availability issues that we've seen in PVC and other materials and the labor challenges you just mentioned, are you seeing any outright demand destruction or is this a matter of projects may

be getting pushed out a few months or a few quarters? I'm just wondering if you could talk a little bit about how your customers have responded to shortages? You talked about substitution earlier, is there a big difference between new construction versus repair and replace or different customer types or regions? Just wondering if you can give any more color there?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Yeah. Anthony, up to this point, we really have seen no cancellations of projects due to material shortages at this point or even price increases at this point. So, the demand has continued to remain very robust as we've gone through this period and we've been able to fulfill, albeit with a lot of work for the last quarter. So, I think, we have certainly some caution out there about where some of these shortages may have a more significant impact in coming quarters. But so far, demand has remained incredibly strong and we've been able to work through these supply constraints.

Anthony James Pettinari

Analyst, Citigroup Global Markets, Inc.

Q

Okay. That's very helpful. And then, apologies if I missed this, but what was your organic volume growth ex-M&A in 2Q? And is there a way to think about what level of organic volume growth is embedded for the guidance for 2021? And then, I understand you're not giving guidance for 2022, but is that kind of 2021 organic growth rate, is there any reason to think it's not directionally sustainable for 2022?

Mark R. Witkowski

Chief Financial Officer, Core & Main, Inc.

A

Yeah. Anthony, thanks. For the quarter, I would tell you it was mostly organic growth. We had our R&B Company, which was our larger acquisition in 2020 anniversary in the first quarter. And then, L & M Supply and Pacific Pipe closed after the second quarter. So, those you should expect to obviously see come through in the back half of the year. Combined, they were about \$130 million in historical annual sales. So, you should see, I'd say, roughly a little less than half or about half of that come through in the back half of 2021. And we won't necessarily forecast the M&A out into 2022 that we haven't completed yet, but obviously, you would expect another half year of those coming through in the first half of 2022.

Anthony James Pettinari

Analyst, Citigroup Global Markets, Inc.

Q

Okay. That's helpful. I'll turn it over.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Thank you.

Operator: The next question is from Nigel Coe of Wolfe Research. Your line is open, please go ahead.

Nigel Coe

Analyst, Wolfe Research LLC

Q

Thanks. Good morning, everyone, and thanks for the question. We cut a lot of ground, so there's not a whole lot to go here. But the incremental margins were clearly very good, especially given the commodity inflation and the price pass-through, it seems like you're getting the margin on that commodity push and that's very unusual. So is

that normal when you see these swings on commodities? So, is it a function of you pre-buying some of the inventory? And I'm curious in the back end of that how you think incremental margins might look in the back half of the year relative to 2Q?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Nigel, I'd say a couple things. Number one, certainly pre-buying has helped us with margins, but probably more importantly than that is our ability to get a lot of these price increases through. We've put in a dedicated team and pricing and category management last year to help drive a lot of that. We felt like many cases we may be lagging in the market in terms of the cost increases that we're hitting and getting that translated to price.

It just so happened that as we started seeing a lot of this inflation hit across all these product categories, our ability to translate that faster, really had a substantial impact as we got into the first half of this year and it was absolutely critical to seeing the performance that you see. We think a lot of that will carry through. Certainly, it is a little difficult to tell how as we start depleting some of the inventory to fulfill current demand and buying at more elevated costs as we would expect to see some type of compression associated with that.

But we do see a lot of opportunity continuing forward with margin enhancement both organically with some of the challenges and the processes that we've improved and certainly looking at some of our private label activity, which is relatively small part of what we're doing, but we'll be rapidly expanding that as well, too.

Nigel Coe

Analyst, Wolfe Research LLC

Q

Great. Thank you. And my follow on is supply chain related and you alluded to this in your commentary around meters and that we've certainly seen particularly acute challenges in, especially in smart meters. So, I'm just curious, are you seeing sort of stable supply in meters here or do you expect there to be a little bit deterioration in the second half of the year, improvements, any color there will be helpful?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Yeah. The supply for certain types of meters right now is really at a premium and we've been prioritizing the available inventory to really serve a good portion of our higher most critical projects out there that would demand that type of meter. So I think, what we're seeing is a little bit of a push in some of the meter projects that will be dependent upon broader availability of those products. So, we will see in that sub-sector that we've got meters particularly for AMI, particularly for a few types of those meters, where that supply is going to be constrained and that will push some of these projects into next year.

Nigel Coe

Analyst, Wolfe Research LLC

Q

Great. Thanks, Steve.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Thank you.

Operator: Our next question is from Mike Dahl of RBC Capital Markets. Your line is open, so please go ahead.

Mike Dahl

Analyst, RBC Capital Markets LLC

Q

Good morning. Thanks for fitting me in. Just wanted to start out as a follow-up to the supply chain question. It seems like by and large, you've still able to serve the customer and serve the products even with some of the challenges, but wondering if you could put [indiscernible] (01:08:41), yeah, maybe quantifying what some of these constraints have meant from a volume standpoint? How much it negatively impacted your expectations for this year? And maybe as a part two of the question, the other thing we've heard recently is some renewed issues on the labor side and an uptick in absenteeism, can you comment on what you're seeing on puts and takes around labor right now?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

I'd share with you that certainly through the first half of this year while the supply has been tight, we've not run into real situations here where we've been unable to meet demand other than a handful of projects that were involving smart meters, so – and that's been relatively immaterial. So we anticipate supply will continue to be tight through the second half. We've obviously provided some guidance here that we'll continue to see demand strong and grow strong and that we'll work through some of that. So that's yet to be determined. We certainly have some cautionary as with PVC, et cetera. So – but for the most part we've been able to work through a lot of that and we anticipate we'll continue to do that.

Now, you had a second question, I'm sorry. Mike, could you repeat the second question? Labor?

Mike Dahl

Analyst, RBC Capital Markets LLC

Q

It was really around labor, yeah.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Okay. Sorry. Yeah. You know, labor...

Mike Dahl

Analyst, RBC Capital Markets LLC

Q

Yes.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Labor has been a real challenge. There's no – yeah, tight labor market for us, we operate you know personally as part of Core & Main, that the situation we operate very lean branches that's been challenging to be able to staff up in every possible area across the country. We continue to provide a lot of incentives to attract talent in here and we've been pretty successful at being able to do that.

When we look at labor for our contractors and our suppliers, they're all having the same challenges right now. And it's hard to speculate whether there's going to be any changes associated with that labor pool and being able to get more people back to work. But we'll continue to work through that. And I think, it'll be a bit of a challenge as we get through the back half of this year, no doubt, but we'll continue to work through it.

Mike Dahl

Analyst, RBC Capital Markets LLC

Q

Got it. Got it. Okay. And then, my follow-up question is still a kind of a related track, but I understand private label is currently small, but when you think about your growth plans and but then balanced by some of the supply constraints that you're seeing, do some of these product availability constraints or global supply constraints, push out the kind of rollout or expansion of your private label efforts?

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

It hasn't been material at this point. So, we continue to build. We've built some supply in here to be able to internally serve a lot of our branches, particularly as fire protection products. So, we've had a comfortable inventory level to carry through on that so far. We're continuing to work through sourcing as well to expand the product offerings that we have in there. So far, we've been able to do a lot of that virtually and it hasn't impeded our progress up to this point. We hope to continue that certainly over the next several quarters.

Mike Dahl

Analyst, RBC Capital Markets LLC

Q

Okay. Great. Thank you.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

A

Thank you.

Operator: There are no further questions on the line. So, I'll hand the call back over to Steve.

Stephen O. LeClair

Chief Executive Officer & Director, Core & Main, Inc.

Well, thank you, all again for joining us today for our first earnings call as a publicly traded company. To close it out, I would like to share a few of the key items that make Core & Main a leading specialized distributor. We are a market leader with size and scale in an attractive and fragmented market. We have a strong value proposition playing a pivotal role in shaping our industry. We have multiple levers for organic growth, continually cultivating ways to grow faster than the market and gain share. We have a proven ability to execute and integrate acquisitions with a large pipeline and additional runway. We are poised to benefit from favorable industry trends in each of our end markets. We have an attractive and resilient financial profile with strong return characteristics.

And to close it out, I'm incredibly proud and want to thank all of our associates for their continued commitment to our customers and our communities, especially given the disruption related to COVID-19, product availability challenges and labor shortages. We are committed to providing our customers with local knowledge, local experience and local service nationwide.

Thank you for your interest in Core & Main. Operator, that concludes our call.

Operator: Thank you for joining today's call. You may now disconnect your lines.

Disclaimer

The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2021 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.