Brunswick Corporation
Second Quarter 2021 Earnings Conference Call
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Presenters
Brent Dahl, VP of IR
Dave Foulkes, CEO
Ryan Gwillim, CFO

Q&A Participants
James Hardiman - Wedbush Securities
Xian Siew - Exane BNP Paribas
Scott Stember - CL King & Associates
Fred Wightman - Wolfe Research
Anna Glaessgen - Jefferies
Kevin Heenan - JPMorgan
Mike Swartz - Truist
Joe Altobello - Raymond James

Operator
Good morning, and welcome to Brunswick Corporation's second quarter 2021 earnings conference call. All participants will be in a listen-only mode until the question-and-answer period.

Today's meeting will be recorded. If you have any objections, you may disconnect at this time.

I would now like to introduce Brent Dahl, vice president, investor relations. Please go ahead, sir.

Brent Dahl
Good morning, and thank you for joining us. With me on the call this morning are Dave Foulkes, Brunswick's CEO, and Ryan Gwillim, CFO.

Before we begin with our prepared remarks, I would like to remind everyone that during this call, our comments will include certain forward-looking statements about future results. Please keep in mind that our actual results could differ materially from these expectations. For details on the factors to consider, please refer to our recent SEC filings and today's press release. All of these documents are available on our website at brunswick.com.

During our presentation, we will be referring to certain non-GAAP financial information. Reconciliations of GAAP to non-GAAP financial measures are provided in the appendix to this presentation and the reconciliation sections of the consolidated financial statements accompanying today's results.

I will now turn the call over to Dave.

Dave Foulkes
Thanks, Brent, and good morning, everyone.

Our businesses had another outstanding quarter. We closed the first half of 2021 by delivering record results as a result of continuing strong retail demand, outstanding operational performance, and success in mitigating material supply and labor challenges. All of our businesses delivered exceptional growth during the quarter.

Our propulsion business continued to realize strong outboard market share gains, leveraging the strongest product lineup in the industry. Our parts and accessories businesses continued to benefit from robust aftermarket demand, driven by elevated boating participation. And our boat business posted its second consecutive quarter of double-digit adjusted operating margins despite significant supply chain, transportation, and labor challenges.

Robust retail demand for our products in the first half of the year has driven field inventory levels to the lowest level in decades at approximately nine weeks on hand. And we are progressing our efforts to efficiently increase capacity across several of our facilities to satisfy orders from our global customer base and begin to replenish the pipeline.

As many of you know, we've also had a busy few months on the M&A front. At the end of the quarter, our Advanced Systems Group significantly expanded its product and brand portfolio by announcing the signing of a definitive agreement to purchase Navico, an industry leader in marine electronics. In addition, we announced in early July that Freedom has expanded into Spain through the acquisition of Fanautic Club. I'll touch on both these exciting transactions later in our discussion.

Given the unique demand and inventory environment, together with continued strong boat usage through the prime season, which drives P&A sales, we have improved visibility on our ability to deliver against an extremely favorable outlook for the remainder of 2021. And consequently, we have increased our 2021 guidance.

Before we discuss the results for the quarter, I wanted to share with you some updated demographic insights through the first half of 2021 and comparisons with the favorable trends we experienced in 2020 versus 2019 in the industry. I'm happy to report that we are not seeing any change in the significant metrics we shared with you during our first quarter earnings call in April.

Brunswick's average boat buyer age continues to be two years younger than the industry average. Additionally, Brunswick's first-time boat buyers continue to be younger than our overall boat buyer demographic and three years younger than the industry. First-time boat buyers are trending more female than they did in 2020, and Brunswick over-indexes to the industry by approximately 800 basis points.

In Freedom Boat Club, the average Freedom member continues to be almost three years younger than our typical boat buying customer and female Freedom members make up approximately 35 percent of our member base. We continue to outperform the industry in attracting younger and more diverse first-time boat buyers, positioning us for very strong growth in years to come. These trends are an extremely important validation of our strategy to secure a healthy future for Brunswick and are also favorable for the entire marine industry.

I also wanted to share with you some awards that Brunswick received during the second quarter that provide more strategic proof points. Brunswick received six 2021 boating industry top product awards, including for the Mercury Marine V12 600-horsepower Verado and the Sea Ray 370 Sundancer Outboard we highlighted recently, but also for our Bayliner Element M15 entry-level boat, BEP's Smart Battery Hub, Attwood's Sahara Mk2 automatic bilge pump, and MotorGuide's Xi3 Kayak Trolling Motor.

Brunswick has also been recognized by Forbes for the second year in a row as one of the best employers for women and ranked second overall in the engineering and manufacturing category. The winners were chosen based on a survey of 50,000 U.S. employees working for companies employing at least 1,000 people in their U.S. operations, and only 300 companies made the final list from the thousands of companies that were considered for the honor.

Finally, Brunswick recently had three employees and a Freedom Boat Club franchisee, Bev Rosella, honored with a Women Making Waves Award from Boating Industry Magazine. We are very proud of these women leaders. As you know, equal opportunity, inclusion, and diversity are cornerstones of our culture.

I'll now provide some second quarter highlights on our segments and the overall marine market. Our propulsion business continues to gain significant retail market share in outboard engines, especially in the higher horsepower categories where we have focused higher levels of investment in recent years. For the first half of the year, Mercury has gained share in each horsepower category over 75-horsepower, with outsized gains in nodes in excess of 200-horsepower.

I'm also pleased to announce that we began shipping the new 600-horsepower V-12 Verado engine in late June and, as anticipated, demand has been extremely strong. We're essentially sold out of the V-12 production slots for the remainder of 2021. And we estimate that just during the back half of 2021, we will sell more outboard engines in this above 500-horsepower class than was sold in the entire prior history of the outboard industry.

Given the surging demand in the current environment and new product launches planned in the coming years, Mercury is accelerating additional capacity investments at its primary manufacturing center in Fond du Lac, Wisconsin in order to maximize its ability to serve the market and capture further share.

Our parts and accessories businesses experienced significant topline and earnings growth and significantly overdrove expectations in the quarter due to outstanding execution, robust aftermarket demand driven by elevated boating participation, and favorable weather conditions in many areas.

The Advanced Systems Group, which has a larger OEM component to its business and also serves certain non-marine segments, benefited from prior year comparisons as a result of Q2 2020 customer COVID-related plant shutdowns. As a result, ASG realized significant growth across all product categories and delivered strong operating margins that were accretive to the overall segment.

Finally, as I mentioned earlier, in late June, our Advanced Systems Group strengthened its product and brand portfolio and significantly expanded its scale and capabilities by announcing the signing of a definitive agreement to purchase Navico. This action will further accelerate our ACES strategy and will enhance our ability to provide complete innovative digital solutions to our consumers and comprehensive integrated systems offerings to our OEM customers. We believe this transaction will close in the second half of 2021.

Our boat segment had another outstanding quarter, posting its second consecutive quarter of double-digit adjusted operating margins despite significant supply chain uncertainty, while delivering output consistent with our production plans for the year. We ended the second quarter with historically low pipeline inventory levels due to consistent strong retail demand for our products.

Given the continued robust retail demand and our dealers' continued desire to take all available product, our 2021 production slots are now sold out for the calendar year, with five brands completely sold out through the 2022 model year. In fact, the sum of our wholesale orders for 2022 model year product is already roughly equal to our projected 2021 full year wholesale boat group revenue.

We continue to hire additional new production employees at most facilities to maintain production consistent with our stated plan. We remain on track with our plans to ramp up and staff the Palm Coast facility and expand our operations at Reynosa and Portugal. Additionally, we've identified capital-efficient investment options to further raise capacity to approximately 50,000 annual production units by 2023, should this volume of product be required.

Freedom Boat Club also continues to exceed our expectations, growing both organically and through acquisition with a young and diverse customer base. With the recently announced acquisition of Fanautic Club and expansion into Spain, Freedom now has 314 locations and

44,000 memberships network-wide and is closing in on 4,000 boats in the overall Freedom fleet, with an increasing percentage of Brunswick product.

The outstanding operational and financial performance I've been discussing has not been without some external challenges that our businesses continue to manage and mitigate sometimes on a daily basis. Our supply chain teams, in particular, have performed extremely well.

Winter storms in late first quarter and resulting power outages in central and southern United States disrupted the supply of oil-based resin and foam products throughout the second quarter, while tight semiconductor supply, raw material shortages and transportation disruption, and resulting cost increases continued to present challenges, which we are actively managing. As a result, our businesses have implemented price increases that are higher than normal, but we believe are generally at the lower end of those implemented across the industry.

The global reach of our supply network and our unique scale in the marine industry, together with our purposeful vertical integration, have so far enabled us to mitigate these challenges and keep our production plans on track for 2021.

I want to thank our supply chain and operations teams as well as our third-party supply partners for continuing to work together to ensure the manufacturing continuity necessary to satisfy our robust market demand.

Finally, labor conditions remained tight in many locations in which we manufacture product. But our talent acquisition teams have been working hard and successfully to add manufacturing and other talent to our teams as we increase production.

Next, I'd like to review the sales performance of our business by region on a constant currency basis, excluding acquisitions. As expected, all regions posted significant sales growth in the quarter versus both 2020 and 2019. Domestic sales grew 55 percent, with international sales up 49 percent, versus prior year. We are seeing strong performance across all international regions, with Asia Pacific still growing despite an extremely strong comparison in 2020.

We continue to experience robust demand around the globe, especially for propulsion products. And we'll be working through backlogs in certain product categories through the remainder of 2021 and into 2022.

This table provides more color on the recent performance of the U.S. marine retail market, comparing the first half of 2021 to same periods in 2020 and 2019. As is usual for this time of year, there's significant noise in the month-to-month SSI data, but the positive market trends continue.

All boat categories reported retail gains in the first half of 2021, continuing the momentum from 2020. Despite more difficult year-over-year comparisons in May and June, the main powerboat segments are still up 17 percent in the first half of 2021 versus 2020 and up 13 percent versus 2019.

Brunswick's year-to-date unit retail performance is generally in line with market growth rates with strength in outboard boat categories. Outboard engine unit registrations were up 5 percent in the first half of 2021, when compared with the same time period in 2020, with Mercury's first half growth more than doubling the market growth rate, resulting in significant market share gains, as I discussed earlier.

As we enter the second half of the year, U.S. lead generation, dealer sentiment, and other leading indicators all remain very positive. Approximately 40 percent of the boats leaving our manufacturing facilities are retail sold, which is approximately three times historical averages. In addition, five of our brands, including Whaler, have all model year 2022 production slots already sold. All these factors give us high confidence in the continuing retail strength as we complete the 2021 selling season and move into 2022.

I'll now turn the call over to Ryan for some additional comments on our financial performance.

Ryan Gwillim
Thanks, Dave, and good morning, everyone.

I'm pleased to share with you the results from another fantastic quarter. To provide perspective in the slides that follow, we have included comparisons in certain places to both the second quarters of 2020 and 2019 in order to highlight the outstanding performance in each of our businesses over the past few years.

When compared with 2020, second quarter net sales were up 57 percent, while operating earnings on an as-adjusted basis increased by 126 percent. Adjusted operating margins were 17.1 percent and adjusted EPS was $2.52, once again setting new all-time highs for any quarter for which we have available records.

Sales and earnings in each segment benefited from strong global demand for marine products, with earnings also positively impacted by favorable factory absorption from increased production and favorable changes in foreign currency exchange rates, partially offset by higher variable compensation costs and increased spending in sales and marketing and ACES and other growth initiatives. Finally, we had free cash flow of 268 million in the second quarter, with a free cash flow conversion of 135 percent.

First half comparisons are equally as favorable. Net sales through the first half of 2021 were up 53 percent when compared with the first half of 2020, and operating margins of 17 percent were a 520-basis point improvement from 2020. This resulted in first half EPS of $4.76 and a very robust operating leverage of 27 percent.

Turning to our segments, revenue in the propulsion business increased 64 percent versus the second quarter of 2020 as each product category experienced strong demand and market share gains. Consistent with the theme from the first quarter, boat manufacturers continue to ramp up production in the second quarter and our increased capacity enabled continued elevated sales to the independent OEM and international channels.

Sales growth was also strong across all product categories when compared to the second quarter of 2019. Operating margins and operating earnings were up significantly in the quarter, benefiting from the factors positively affecting all of our businesses.

In our parts and accessories segment, revenues increased 42 percent and adjusted operating earnings were 46 percent up versus the second quarter of 2020, due to strong sales growth across all product categories. Adjusted operating margins of 23.2 percent were 60 basis points better than prior year quarter, with significant sales increases driving a robust increase in adjusted operating earnings.

Sales growth was also very strong across all product categories when compared to the second quarter of 2019. This aftermarket-driven annuity-based business continues to benefit from more boaters on the water, which is being augmented by flexible work schedules allowing for more leisure time, with the OEM component of the business leveraging investments in technology to take advantage of increased demand from boat builders as they continue to increase production.

As anticipated, our boat segment results benefited the most when compared with the second quarter of 2020 due to last year's COVID-related plant shutdowns and production ramp-ups. Sales were up 80 percent and operating margins were 10.5 percent for the quarter, the second straight quarter this segment has delivered double-digit margins. Each brand had strong operational performance, executed their aggressive production plan, and contributed to the overall segment's success in the quarter.

When compared to the second quarter of 2019, sales were up 22 percent, and operating margins were up 160 basis points, further illustrating the foundational improvements that have been made in this business.

Operating earnings were also positively impacted by the increased sales and the lower retail discount levels versus 2020. Freedom Boat Club, which is included in Business Acceleration, contributed approximately 3 percent of the segment's revenue and a margin profile that continues to be accretive to the segment.

Turning to pipelines, our boat production continues to ramp consistent with our plans to produce approximately 38,000 units during the year. Despite producing almost 10,000 units in the quarter, which is up 5 percent from the first quarter, retail outsold the wholesale replenishment by more than 7,000 units, bringing dealer inventories to an all-time low of approximately 7,400 units. Our boat brands ended June with under 10 weeks of boats on hand, measured on a trailing 12-month basis, with units in the field lower by 50 percent versus same time last year.

Given our view that the industry retail market will be up high single-digit percent for the year, we believe that retail will outpace our production targets resulting in our year-end weeks on hand to be lower than year-end 2020 by several weeks. We continue to work with our brands to unlock additional near-term capacity through automation, labor, and select capital initiatives, including the capacity actions announced earlier in the year related to our Palm Coast, Reynosa, and Portugal facilities, which will begin providing benefits by the end of the year.

2021 is shaping up to be another year of robust earnings and shareholder returns, with pronounced margin increases and substantial free cash flow generation resulting from our outstanding operating performance in a healthy marine market. Given the enhanced clarity on our ability to drive growth in upcoming periods, we are providing the following updated guidance for full year 2021.

Without including the potential benefits from the Navico acquisition, we anticipate the U.S. marine industry retail unit demand to grow high single-digit percent versus 2020; net sales of between $5.65 billion and $5.75 billion; adjusted operating margin growth between 150 and 180 basis points; operating expenses as a percent of sales to remain lower than 2020; free cash flow in excess of $450 million; and adjusted diluted EPS of approximately $8.

We're also providing directional guidance regarding the third quarter, where we anticipate revenue growth of mid-teens percent and EPS growth of high single-digit percent. Note that we believe that the Navico transaction, once closed, will be earnings neutral to 2021 as we anticipate Navico's post-closing earnings to offset the incremental interest incurred as a result of the deal.

Next, I'd like to provide some perspective on our 2021 performance against 2020 and 2019 by looking at first half and second half results. The revenue cadence for 2021 will look more like 2019 and 2018 than it did in 2020. The first half of every year has additional production days as the second half includes model changeover and holiday shutdowns.

However, first half of 2020 was materially impacted by the COVID-related plant shutdowns. This resulted in the first half of 2021 comparing very favorably to 2020 in all of our businesses due to higher production volumes, with additional earnings tailwinds from improved absorption, favorable foreign currency comparisons, and favorable changes in customer mix in our propulsion business. These factors far outweighed the headwinds from supply chain challenges, inflationary pressures, and higher variable compensation expenses experienced during the first six months of this year. Our first half performance this year also exceeded 2019 in every metric.

As we head into the second half of 2021, we will face more difficult comps to 2020 as the company recorded record-high EPS over the same period last year, and we will continue to be challenged with supply chain constraints and increasing input and freight costs.

Although we are taking price increases across our businesses, we also anticipate moderated sales mix with propulsion sales trending more towards core OEM customers, more typical seasonality in the P&A business, and a higher percentage of overall growth in the boat business, increased spending on ACES and other growth initiatives, smaller benefits from currency and absorption, and a higher tariff impact.

However, despite more challenging second half comparisons, this continues to be a growth story. We anticipate expanding top-line in the second half by double-digit percent versus the second half of 2020, which will be more than 40 percent greater than 2019 with higher earnings as well.

I will conclude with an update on certain items that will impact our P&L and cash flow for the remainder of the year. The only meaningful update relates to our effective tax rate for the year. Due to some fantastic branch restructuring work by our tax team and business units, we now believe our effective tax rate for 2021 will be approximately 22 percent, which is slightly lower than our estimate from our April call.

Similarly, and putting aside the financing related to the Navico transaction, our capital strategy assumptions have not materially changed. In the past few weeks, however, we have taken several steps to strengthen our overall liquidity and shareholder return profile. We extended and expanded our revolving credit agreement, which is now in effect through July of 2026, which now provides for $500 million of borrowing capacity, an increase of $100 million.

In addition, our board of directors increased our share repurchase authorization earlier this month, and we now have over $400 million approved for repurchases, which we plan to systematically deploy consistent with our capital strategy. These moves follow our substantial 24 percent dividend increase approved in April as we continue to balance desired increases in shareholder return and investment in growth initiatives.

We now anticipate spending 270 to $300 million on capital expenditures in the year to support and, in some cases, accelerate growth initiatives throughout our organization. This slightly increased planned spending is primarily related to the Mercury capacity expansion that Dave discussed earlier.

I will now turn the call back over to Dave to continue our outlook comments.

Dave Foulkes

Thanks, Ryan. At our April call, we felt that 2021 was setting up to be an outstanding year for all of our businesses. And the combination of continued robust retail demand during the first half of the year and solid operational execution by our businesses has us squarely on track to deliver against our operating and strategic priorities.

Our top priority for the propulsion segment continues to be satisfying outboard engine demand from new and existing OEM customers and expanding market share, especially in dealer, saltwater, repower, and international channels. We are continuing to invest heavily in new product introductions and industry-leading propulsion solutions that we project will enable top line and earnings growth far into the future. And we've also recently taken the decision to accelerate the introduction of incremental capacity.

Our parts and accessories segment remains focused on optimizing its global operating model to leverage its distribution and position of strength in areas of battery technology, digital systems, and connected products in support of our ACES strategy.

We look forward to closing the Navico deal and beginning thoughtful integration into the ASG business. We will continue to focus M&A activity in parts and accessories as we look for opportunities to further build out our technology and systems portfolio.

The boat segment will build on its first half successes by continuing to focus on operational excellence, improving operating margins, launching new products, executing capacity expansion plans, and refilling pipelines in the very robust retail environment.

I wanted to leave you today with an update on the progress we've made towards the “Next Wave” of the company's strategy, highlighted during our virtual Investor Day in May and our recent press releases.

In addition to the Navico and Freedom Boat Club transactions, and the start of shipments of the V-12 600-horsepower outboard, which I've already discussed, proof points in the quarter included the launch of the My Whaler and Sea Ray+ apps for Apple and Android users, which advances the ACES Connectivity strategy by improving the boat ownership experience, reducing friction across the entire ownership journey. The initial reception of these products is extremely promising, with more than 2,000 accounts created in the first few weeks and a star rating of 4.9 out of five.

And the launch of the Heyday H22 Wake boat, a new leading-edge, wake-surf model, signaling a doubling down on this fast-growing brand appealing to a younger demographic. This model is already sold out through mid-2022.

We're tracking well against all our Next Wave strategic goals, including the electrification initiatives outlined in May.

Finally, I want to once again offer a heartfelt thanks to our global employee population for all their dedication, effort, and sacrifices during what is still a challenging time for our families and communities. Your hard work has enabled us to seamlessly execute our strategic plan and significantly outpace our initial growth and profit expectations.

We'll now open the line for questions.

Operator
Ladies and gentlemen, we'll now have our question-and-answer session. If you would like to ask a question, please press star one on your telephone keypad. A confirmation tone will indicate that your line is in the question queue. You may also press star two if you would like to remove your question from the queue. One moment, please, while we now poll for questions.

Our first question comes from James Hardiman with Wedbush Securities. Please proceed with your question.

James Hardiman
Hey. Good morning. Thanks for taking my call. First, just two very brief clarifications. The slide, I think, it's 22, the first half versus second half--I'm trying to take out my ruler here, but it looks like operating income is about flat second half of this year versus second half of last year. But then, Ryan, I thought--you may have said that earnings are higher year-over-year there. So, maybe just a clarification there. And then is production up versus how you had previously guided it for 2021?

Ryan Gwillim
Hey, James. Good morning. Yes, second half operating earnings are indeed up over 2020. EPS is up a little greater than operating earnings, but operating earnings themselves are indeed up in the second half. And then production, I would tell you is right on track to what we had guided to earlier in the year. And despite a lot of late nights and hard work with our supply chain and other folks, we're producing exactly as we anticipated.

James Hardiman
Okay. Perfect. And so, that leads me to my broader question as I think about supply chain and what the bottlenecks are, which is, I think, going to be the--it already been, but I think will continue to be the theme of this second quarter earnings season. Obviously, we've heard from some of your power sports peers, it's clear that in a lot of cases, their plants are not necessarily at full utilization because their supply chain is limiting the flow of parts and components into those plants.

Given that your production assumptions seem to be pretty consistent, it doesn't seem like that's necessarily the issue for you guys. I guess, is that an accurate characterization of the current situation? And that it's more of a cost issue rather than a part and supply availability issue?

Dave Foulkes
Hi, James, it's Dave. Yeah, I would say that's a pretty good characterization. I would say that we deal with the kind of new challenges every day and every week. And so far, we've been able to mitigate them very successfully. I would say the impacts to us really are certainly cost, but we are pricing to cover that. And I did note that we believe our price increases are at the lower end of the industry, but certainly enough to cover the increased cost.

I would say that there is productivity impact, though. We are maintaining our production, but I would say that not always in the--we have some boats and other things that we have to take off the line, wait for parts, bring back on the line. Those kinds of production disruptions just mean that there is some productivity impact. But so far, we're able to continue production schedules with some of those kind of manageable impacts.

James Hardiman
Got it. And then, just lastly for me, I don't know if this is even possible just given all the moving parts, how big of a cost or margin impact do you think that is for you guys this year? Again, obviously, there's some top line impacts, although those seem to be smaller for you guys than all of the expenses associated with expediting and inflation and all those sorts of things.

Dave Foulkes
Yeah. Ryan, I don't know if you have a good idea. I think, clearly, we are, on an annual basis, pricing to cover inflation as we understand it right now. Obviously, we're halfway through the year, so we don't necessarily understand everything. But our plan is to continue to do that. I would really measure this in kind of points of productivity, but I don't have a ready kind of translate into dollars. Ryan, I don't know if you--.

Ryan Gwillim
--No, the only thing I would mention, James, is obviously the boat business continues to deliver on margins. And you've seen the guidance creep up. I think the number 10 has made an appearance, the official guidance for the rest--for the full year at 10 percent. So, like Dave said, we're covering over with price, but it certainly is a bit of a headwind.

James Hardiman
Real encouraging. Thanks, guys.

Dave Foulkes
Thank you. Thank you, James.

Operator
Thank you. Our next question comes from Xian Siew with Exane BNP Paribas. Please proceed with your question.

Xian Siew
Hi, guys. It's Xian Siew. Thanks for taking the question. Just on the pipeline. So, it's down a bit quarter-on-quarter and it seems like availability is still maybe not fully there. Do you think that the industry has enough availability retail could have been--like, I guess, how much higher could retail have been if there was enough supply? Is there any way to quantify that?

Dave Foulkes
Well, in the--thanks for your question. In the last call, we did indicate that we believe that on an annual basis, retail would likely be up, you know, I would--several more points without retail constraints. It is very clear that people are buying what we can produce at this point in the year. Now, we are--as we begin to get through the prime selling season over the next couple of months, we will be planning to build inventory again, assuming that the market develops as we expect.

So, from nine weeks now, we'd expect to be kind of low to mid-teens by the end of the year. But right now, and probably through most of the year, it certainly is a constrained marketplace. I don't know if I could identify exactly what the points are, but I would say there's several points under the free demand--under the free supply.

Xian Siew
Okay. Thanks. And then, on Freedom, congrats on the acquisition in Europe. Just wondering how big the opportunity could be internationally and how those kind of boat clubs are received--those concept received in Europe. Any differences between those models in Europe versus the U.S.? Any kind of initial learnings there?

Dave Foulkes
Yeah. I would say that the appeal is equal in the right marketplaces. So, for example, Spain, France, in some parts of Italy, certainly the UK, Portugal, southern Portugal, those are all areas where you have very strong interest in boating, enough people with financial capability to join a boat club. The concept is a little earlier in Europe than it is in the U.S. But really, when you think about it, Freedom Boat Club was around a long time before we bought it and really had reached an inflection point, just probably a couple of years earlier.

So, as knowledge of the model becomes wider and as we professionalize that space with the same toolkit that we're using in the U.S., we think that the potential is really substantial. Obviously, Europe is our second biggest market for Brunswick as a whole. Very, very long history of recreational boating both in the Mediterranean and kind of near shore Atlantic.

So, we'll be working quickly to begin to establish some of the tools and techniques, marketing, kind of professionalize the space. We think the potential is very, very substantial, well beyond where we are right now.

Xian Siew
Great. Thanks, guys.

Operator
Thank you. Our next question comes from Scott Stember with CL King & Associates. Please proceed with your question.

Scott Stember
Good morning. And thanks for taking my questions.

Ryan Gwillim
Hey, Scott.

Scott Stember
Yeah. I think I probably know the answer to this just based on the commentary, but just want to make sure, have you guys--would the lead times continue to get extended ahead of any relief on the supply side? Have you seen any accelerated rates of customer cancellations on boats?

Dave Foulkes
No, we haven't seen anything at all. We know that some of our channel partners have kind of potential second and even third customers signed up for boats in case the lead customer has a change of mind. So, we're not seeing anything in terms of increased cancellations.

Scott Stember
All right. And I know it's a little bit further out and probably one that you guys want to give guidance on, but just your initial thoughts on what 2022 could look like, whether from a retail perspective for both. So, do you think it could be an up year? And if so, how much?

Ryan Gwillim
Hey, Scott. Yes, well, it's probably a bit premature to do a market call on next year, but we do think retail will grow next year. That's our belief still. We talked about that on investor day as well as the first quarter call.

In terms of guidance, we're not going to update the guidance that we gave on the Navico call. Obviously, 8.25 to 8.75 was our investor day outlook for '22. And then, we said that Navico we anticipate would add a net 50 cents or so to that figure. And that's Navico's earnings less the anticipated additional financing costs.

So, that--none of that has changed. I would tell you, though, that obviously, the jumping off point for '22 looks like it's going to continue to be a little higher because '21 is coming in nice and strong. So, no real changes at all on our view to '22.

Scott Stember
All right. And just a last question. Last quarter, you talked about--within ASG, you talked about new plans to install about 15,000 of the Fathom e-power systems for internal combustion generators I guess by 2023. Can you talk about the timing of that and how significant that could be?

Dave Foulkes
Yeah. So, we're on track with that plan. The 15,000 represented two things really. It represented the Fathom and Fathom-type generator replacements for marine applications, plus the replacements of generators in recreational vehicle applications, and we're actively doing that.

We have a number of ASG team members located on site at RV manufacturers installing our advanced battery systems. And they've become so popular that some of the RV manufacturers are changing their standard content to include this battery system instead of a generator. And as soon as you move from being an option to being standard, that somebody has to deliberately change, the volumes go up. Yeah, so, we're very much on track.

Our Advanced Systems Group Connect business, ASG Connect, which you might remember is the part of the ASG business that works with both boat builders and RV manufacturers and specialty vehicle manufacturers to integrate our systems, was up 133 percent in the first half of the year. So, it's a very in-demand service, and people are taking advantage of this great portfolio of technologies that we have and our ability to integrate it on their behalf.

Scott Stember
Excellent. That's all I have. Thanks.

Ryan Gwillim
Thanks, Scott.

Operator
Thank you. Our next question comes from Fred Wightman with Wolfe Research. Please proceed with your question.

Fred Wightman
Hey, guys. Good morning. Thanks for taking my taking the question. I was wondering if you could dig into the Mercury capacity a little bit more that you outlined. Is that incremental to sort of what you had hinted at last quarter?

What type of capacity uptick are you sort of planning for? Where is it targeted sort of that mid-horsepower, high horsepower? Anything that you could provide there would be super helpful.

Dave Foulkes
Yeah, sure. Thank you for the question. Yeah. So, yeah, it is all incremental to what we'd originally talked about, and it's being driven by very strong demand for our products. It is roughly the same additional incremental capacity as the prior incremental capacity that we put in during 2018 and 2019.

And I would say, yes, it is overweighted to mid- to high horsepower engines and it's mainly in our Fond du Lac facility, which is where we produce most of our high horsepower engines and also in the supply base that supports it. We have to make sure that our supply base is scaled just the same as our internal facilities are.

But just kind of connecting a few things. We remain in very active discussions with potential new customers for Mercury. But our priority, obviously, is to support our existing OEM and other customers. And what that means right now is all of our existing--or the vast majority of our existing customers are ramping up their production and they need more engines from us.

That means we have to be careful about how we add new customers. It also means--and I'm kind of connecting with something that Ryan said earlier about the second half of the year that we don't have as many engines right now as we would like to provide to dealers for repower, for example, which is a very profitable channel for us.

So, top priority is to serve our existing customers whose demands are going up and up and up. And so, it's the right time for us now to add more capacity so that we can continue to bring on board new OEM customers, and also have enough engines so that we can satisfy those high-margin dealer repower and international channels, commercial channels, et cetera, that tend to have to fall after some of the big OEM customers as we satisfy their demand.

Fred Wightman
Okay. That makes sense. And just another capacity question on the boat side. I think that you mentioned you'd be at 50, 000 units in terms of capacity by '23 now. I think that number in the past was something in the low-40s that you were targeting. So, sort of a two-part question.

Are those numbers apples-to-apples? And then, secondly, when could those start to hit? Is that something that could show up later in '22? Or is it really a '23 story?

Dave Foulkes
Yeah. So, this is new again. So, we had--we have detailed plans that we're executing. And in fact, we're along way--along the way now to implement that capacity around 43 to 44,000 units, which is up from the kind of high 30s that we had earlier or last year, if you like.

So, that is reopening the plant that we call it the Flagler or Palm Coast sometimes and then expanding our Reynosa and the Vila Nova facility in Portugal. That drives up to 44,000, but it is very clear that with the pipelines where they are and with retail demand where it is, and with things like Freedom Boat Club expanding really, really quickly and demanding more and more boats, that might--that 44,000 might not be enough.

And so, we have begun a series of steps to increment that 44,000 up to around 50,000 that will require modest additional investment, but is, in most cases, not a significant footprint increases. In a couple of cases, there is footprint inside mostly our existing kind of land. But yeah, this is--the 44 to 50 is incremental and we'll be working on making sure that we can introduce it as quickly as we can, but 2023 is currently the target.

I would say that what we--I don't know if we'll need 50,000 units, but I know that the signs are that we might, and I would not want to lose market share, certainly don't want to short Freedom, which is growing like crazy. So, we think it's prudent at this time to cost effectively build out that additional optionality.

Fred Wightman
Perfect. Thank you.

Ryan Gwillim
Thank you.

Operator
Our next question comes from Anna Glaessgen with Jefferies. Please proceed with your question.

Anna Glaessgen
Hi. Good morning. Thanks for taking my questions. First, on the Verado with production sold out through '21, could you maybe contextualize this versus what your preliminary expectations were the performance of that engine?

Dave Foulkes
Yes. Thank you for the question. Yes. The demand for the V-12 is going--is very high. I think it's attracting a lot of interest. It's causing a number of boat builders to rethink their portfolio and put in outboards where they might have put in inboard engines on bigger boats. So, yes, the demand is certainly higher than our original expectations. So, we'll kind of work our way through this second half of the year.

I think the comment that we made earlier was--without being very explicit about numbers to indicate--earlier, there were some other higher horsepower engines in the marketplace, but this is different. As I mentioned earlier, we expect in the back half of this year we'll produce more outboard engines above 500-horsepower than we'll produce in the entire prior history of the industry.

So, the scale of this engine at this horsepower level is substantially higher than anything else. And yeah, we're seeing very robust demand and a lot of interest, and it is certainly higher than we originally anticipated.

Anna Glaessgen
Great. Thanks. And then, turning back to the capacity investments to reach that 50,000 boat unit number. So, I think in the deck, it was kind of presented as you've identified the ability to ramp to that. I guess, are you committing to kind of those investments? Or when would that decision have to be made in order to ramp up to that by '23?

Dave Foulkes
So, the investments are phased over time, and we can continue to monitor the marketplace and any other developments that are relevant. There are some early pieces of investment that we'll be funding even as early as this year, but it will be spread over the next couple of years.

Anna Glaessgen
Okay. Great. Thanks.

Operator
Thank you. Our next question comes from Matthew Boss with JPMorgan. Please proceed with your question.

Kevin Heenan
Hi. This is Kevin Heenan on for Matt. Congrats on a strong quarter.

Dave Foulkes
Thanks, Kevin.

Kevin Heenan
I just wanted to ask about the boat segment margins. Strong again this quarter, in the double digits. I was wondering if you could maybe rank order the drivers of the boat segment EBIT margin strength and how you're thinking about the sustainability of those drivers as we move out of the pandemic environment. Thanks.

Ryan Gwillim
Hey, Kevin. Thanks for the question. It's pretty straightforward, to be honest. It is volume, improved volume, which allows for better absorption. It is operating more efficiently throughout the facilities. And at least in the last couple of quarters, it is a bit of lower discounting environment given that we do not need to provide support or much support to the dealer network in order to sell product. But in general, it is certainly those factors.

The other thing I would mention is, the new products that are coming out that we talked about on the investor day, 122 new or refreshed products, all of those are being designed for manufacturer at a higher margin than the products that they are replacing. And that's something you've heard from us for years on the Mercury side as we roll out new engines, but that same philosophy has now moved to the boat business. And the new products coming out are really going to be margin drivers for us.

Kevin Heenan
Okay. And if I could ask one follow-up just on the P&A side. Just could you talk about the long-term opportunity for this business now that you're adding Navico? I think you've cited a 6 billion market in the U.S. I mean, how best to think about your ability to scale and remaining drivers of opportunity here, I guess, both in the U.S. and globally? Thanks very much.

Dave Foulkes
Thank you. No, great question, yeah. So, I think Navico was an important addition to our portfolio and our brands. It enables us to do a lot of things, but there are plenty of other opportunities in that marketplace for us to build out our portfolio.

I would say that as we have noted, our Advanced Systems Group currently sells about 25 percent of its products into recreational vehicle and specialty vehicle. And the 6 billion is only the marine portion of P&A.

So, as we become more and more successful in, for example, installing those advanced battery systems into a recreational and specialty vehicle, we feel as a right to win some other areas of RV and specialty vehicle, leveraging the same or modified systems and technology that we use in marine. So, I would say that there's room to run in marine, certainly, plenty of room to run in marine, but also room to run in adjacent spaces as well.

Ryan Gwillim
And Kevin, one thing, just to put a bow on this. One thing that we're proving out is the growth of our P&A business and the strength then of the aftermarket annuity revenue and earnings that that business provides. This is going to be approximately $2 billion and still growing organically starting in '22, which is obviously four or five times larger than it was coming out of the downturn in 2008, 2009. So, just a reminder that the mix of our businesses continues to trend positive and towards the aftermarket and countercyclical portions of our business.

Kevin Heenan
Good. Thanks very much, guys.

Operator
Thank you. Our next question comes from Mike Swartz with Truist. Please proceed you’re your question.

Mike Swartz
Hey, guys. Good morning. Just maybe a broader question about how you think about product development and launch strategy, maybe portfolio strategy within the boat business just given some of the dynamics we have in the market today with capacity constraints and supply chain issues and just elevated demand and backlogs out until '22. I mean, how does that play into your strategy in the near term and maybe longer-term?

Dave Foulkes
I think--yeah, good question, Mike. We always believe that over the long run, new product wins. So, we are not pausing new product introductions, not pausing up our product development activities. But because of this somewhat unique situation, except in some really exceptional situations where we just--we can't get parts or something or one of our suppliers says, you can either have a production lag or a development part.

But in terms of what our intention is, is we know in this marketplace, new product wins over the long-term, and we will continue to invest and not intentionally at least, pause any of our key programs.

We--one of the ways that we are attracting into--attracting new people or people into new boats is by providing new technology, by providing new models with content they can't get in the pre-owned marketplace, new form factors, new wholes, new connectivity, new solutions.

So, I think we have to continue to differentiate new product from pre-owned product, both from a design and aesthetic perspective and from a technology content perspective, and we will continue to do that.

I'm particularly excited about some of the stuff that's coming out, we've already seen them. The H22 from Heyday has been--I mean, the reception has been great. It's really--as you look at the wake sports market, it's really the value portion of that market that's been really growing. And so, the ability to put a new product into that marketplace already sold out through 2022, it's been excellent. And we will selectively evaluate expanding our portfolio into areas that we think where we can really make a difference.

So, that's essentially our philosophy. New product wins over the long-term. We need to differentiate new product from pre-owned product. And we'll get into more and more white space is where we think the customer base is moving.

Mike Swartz
Okay. Wonderful. And maybe a question for Ryan just on some of the commentary around product mix, I guess, being less favorable in the back half of the year. You've talked about some of your premium boat brands with extended backlog. You've talked about the launch of the V-

12 engine that will pick up pace here in the back half of the year. So, I guess, what exactly is weighing on product mix? Is it just OEM--just the OEM mix within the engine business?

Ryan Gwillim
Yeah. It's really two things, Mike. It's the way the forecast looks for the rest of the year, our kind of core OEM customers look to be getting more percentage of the engines than potentially our dealer network or international markets, which tend to be a little bit richer in terms of margin.

And then, just as a company overall, the boat business continues to be a kind of a consistent chunk of the revenue and earnings. And as P&A exhibits a little bit more normal seasonality really in the fourth quarter, that's just kind of a mix headwind.

But again, these are--this is a growth story, even in the second half. We're comping against the best second half that the company ever had last year and we're still growing topline and earnings. So, we wanted to give a little bit more detail around it, but it's still a very positive story, trending into '22, which, again, we feel is going to be another fantastic year.

Mike Swartz
All right. Thanks. That's it for me.

Ryan Gwillim
Thanks, Mike.

Operator
Thank you. Our next question comes from Joe Altobello with Raymond James. Please proceed with your question.

Joe Altobello
Thanks. Hey, guys. Good morning.

So, first question, want to kind of delve into your industry outlook, which you revised today to up high singles for the year. And I think based on the first half, it implies roughly flattish industry retail in the second half. Is that a little bit aggressive given the tougher compares that we'll be facing as well as the inventory situation as it seems like supply is the bigger issue rather than demand right now?

Ryan Gwillim
Yeah. I mean, Joe, that's how the numbers are shaking out. I mean a very strong first half. Your math is right, kind of a flattish back half, which is flat to a very strong back half, obviously, last year post-COVID.

But again, our retail sales are up just from boats leaving the facility. So, 40 percent of our boats leaving our facilities are retail sold, which is--continue to buoy that number and keep it where we think it's going to land. But yeah, that's exactly the thought process.

Dave Foulkes
Joe, we also do--we would expect to build some weeks on hand from now through the end of the year. As I mentioned, we're at nine right now and hope to be in the kind of low to mid-teens. So, we are building inventory through a part of the season that obviously, where the demand naturally seasonally drops a bit. So, yeah, trying to get the right balance is a bit tricky, but we think it's going to end up in the high singles.

Joe Altobello
Okay. Great. And just shifting over to outboards. Your market share gains there have been obviously very impressive for years now. It does sound like we could see additional capacity or additional supply, I should say, from your largest competitor coming in the next few weeks. Might that impact or have an impact on the pace of your share gains in the second half?

Dave Foulkes
Well, I think that if you look at our--what we just described--when we talk about share gains, we're really talking about OEM share gains mostly. And we're continuing to drive those forward and make sure that we prioritize our OEMs. A lot of the share gains that we're seeing are from OEMs that we already signed up. So, we have commitments from OEMs.

I would say that, in contrast to some of our competitors who have come out and said, they are not adding more capacity, we have come out and said, we are adding more capacity. And I think if you're an OEM looking to the future of your business in a growth environment, you would want to go with a person who says they're going to add capacity, and has demonstrated that indeed, they do.

So, I think we have a very strong--we have very strong momentum. And I think that our story around capacity and product is very compelling and will lead to continued share gains.

Joe Altobello
Great. Thank you, guys.

Ryan Gwillim
Thanks, Joe.

Operator
Thank you. Ladies and gentlemen, that is all the time we have today for questions. At this time, we would like to turn the call back to Dave for some concluding remarks.

Dave Foulkes

Well, thank you all very much for joining us. I really appreciate it. We're very excited about the continuing very strong operational and financial performance of the business. Obviously, we'll continue to work hard with our supply chain partners to make sure that we continue to mitigate issues, including things like COVID and the Delta variants.

We're also very excited about the significant early proof points that we've been able to establish on our Next Wave and ACES strategies. It's going to be a busy second half. We'll be welcoming about probably 2,000 employees of Navico to the Brunswick team when we close the deal later this year. And we look forward very much to delivering on the synergies and opportunities between our two businesses.

So, look out for more strong performance. Look out for some more exciting developments as we work our way through the next quarter. Thank you all very, very much.

Operator
Ladies and gentlemen, this concludes today's webcast. You may now disconnect your lines at this time. Thank you for your participation. And have a great day.