The Scotts Miracle-Gro Company NYSE:SMG

Company Conference Presentation

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James D. King
Chief Communications Officer, Executive VP & President of The Scotts Miracle-Gro Foundation

Thomas Randal Coleman
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Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Presentation

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Okay. Well, hello, everyone. Thank you for joining us. My name is Joe Altobello, equity research analyst here at Raymond James, covering the household, personal care and leisure industries. We are very pleased to have with us today the senior management team from Scotts Miracle-Gro, including Chief Financial Officer, Randy Coleman; and Chief Communications Officer, Mr. Jim King.

Scotts is the unquestioned leader in the U.S. consumer lawn and garden product sector. While its Hawthorne hydroponics business has been on fire, no pun intended, driven by the expanding legalization of and demand for cannabis globally. We're going to employ a bit of a hybrid format today, with Randy kicking things off with an update on current trends. Hopefully, everyone saw the press release that Scotts issued last night in which they raised fiscal '20 guidance once again. At which point, we'll then move into a fireside chat format.

So with that, let me hand things off to Randy for some remarks.

Thomas Randal Coleman
Executive VP & CFO

Thank you, Joe. And I trust that you can hear me?

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Yes.

Thomas Randal Coleman
Executive VP & CFO

Well, I think you cannot see me?

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

No, unfortunately.

Thomas Randal Coleman
Executive VP & CFO

All right. So we're having a little technology glitch, which my kids would tell you, is not to be unexpected with me, but we'll carry on anyway.

We do not have a presentation for today, but we do have a few scripted dots to share with everyone before we get to Q&A.

So given that, I think it's certainly been a challenging time for the world and our country this year, but we've been very fortunate to be in the businesses that we're in, as they're considered essential, and we've performed extremely well under the circumstances, with strong focus, execution and agility.

As you know from the press release last night, we caught up our numbers again to over 30% sales growth and about $7.25 of EPS for 2020. Total company sales growth assumes almost a 25% increase for the U.S. and about 60% for Hawthorne. We also expect free cash flow, which we define as operating cash flow with less CapEx, to now approach $500 million for the year, as we've struggled to build our inventory since practically everything we buy and make is being shipped out as soon as possible.

The word unprecedented is probably being overused right now, but it's also accurate for us. We've struggled in predicting how high is high this year, and let me provide some context on the reasons why.

In the U.S. business, we started the year well, even before COVID began to affect the country. Our Q2 POS was up about 20%. April was down 8%, as home centers were careful about ordering and driving traffic in the weeks after COVID hit the U.S. Then business picked up in May, as consumers became more accustomed to working from home, and focused on their yards, and May was up 44%. We expected June to slow down as we always, at least until this year, see a big drop-off in consumer activity after mid-June.

But this year, it was different. Our string of $100 million weeks continued until the end of the month, and June POS was up 50%. While the POS curve has returned to normal since then, the year-over-year increases are still almost 40% in Q4. So we clearly underestimated the continued strength of POS and consumer engagement over the last few months.

The more recent impact on our U.S. sales relates more so to retailer attitudes. Across the board, retailers continue to push lawn and garden and are gearing up for a huge fall season, and there are no obvious constraints on inventory or ordering. As a result, we now expect year-end inventories to be at least 20% higher than last year on September 30. This retail inventory build was not anticipated in our guidance in late July.

This also creates a line of sight to a big Q1 and even beyond Q1 until we begin to comp big numbers in Q3 of next year. We're optimistic about U.S. consumer next year for several reasons: first, continued consumer engagement and a work-from-home environment; Scotts' marketing focus on one-to-one relationships with consumers throughout the entire year; strong retailer push in our category, including anticipation of a more promotional approach in 2021; SMG has continued to support of our retailers' e-commerce platforms as well as our own; and we're building inventory to improve service and capture sales that we believe we missed out on in 2020.

Switching to Hawthorne. Q4 sales continue to grow versus a year ago, and we now expect September to be our largest sales month ever. We'll be at the top end of our sales guidance from late July, and we'll exceed our 10% operating margin rate for 2020.

Looking ahead to next year for Hawthorne, we remain bullish given the consistent wholesale and retail prices in the marketplace, our growth and expected sustainability in consumer demand and our belief in significant market share gains during the year. While it still remains too soon to provide specific guidance today regarding next year, we are optimistic about the continued commercial opportunities for both of our major businesses through March of '21.

Our service performance this year was below our expectations and retailer expectations at certain points in the year for both of our segments, and we believe we left about $200 million of sales on the table by just not being able to keep up. We also know we have about $1 per share of expense tailwinds in 2021 from incentives and P&L investments that we made over the last few months of fiscal '20. I'll provide specific P&L line item guidance when we have our Q4 earnings call on November 5.

After talking about the numbers, I also want to emphasize how well we've taken care of our people this year. We added 50% premium pay for frontline workers during the onset in the first couple of months of COVID, and we continue to pay 50% premium in [hired] spots. We also initiated to maintain enhanced cleaning protocols, and we manufactured and gave away face shields to organizations across the country. And more recently, we decided to pay annual bonuses to hourly associates, who are not typically eligible for our annual bonuses, and we're also dramatically increasing our charitable giving in our communities. We're grateful for the support from our consumers and retailers this year, and we know we're fortunate to be in fast-growing categories, when much of the country is still struggling. So thanks for listening today, and I'll ask Joe to kick off the Q&A. Thanks a lot.

Question and Answer

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Great. Thank you, Randy. That was very helpful. So I want to begin by asking about 2000 first. It's, obviously, been an unusual year to say the least. But for Scotts, financially, I think it might be your greatest year ever. If someone were asleep for the past 6 months, and were -- and then they woke up to see their -- your U.S. consumer sales up 25% and Hawthorne up 60%, I'm not sure they'd believe it, but here we are.

So could you help us understand what's been driving that growth since it is so much above what you've historically done in the past? Is it people spending more time at home? Is it the fact that your retailers were deemed essential and were able to remain open? Is it a combination of those things? So help us understand what's been driving this super growth in 2020?

Thomas Randal Coleman
Executive VP & CFO

Sure. So I'll start with the U.S. business. And like I said in my prepared remarks, we started off the year really strong. We knew we had listing gains within and beyond the Big 3. We had a little bit of pricing that's going to be about 1 point for the year. So we had a lot of optimism coming into the year. But things did change quite a bit once COVID hit the country.

April, I think everybody pulled back a bit. I know definitely that the home centers did, and they were trying to do the right thing, be respectful, take care of their associates and not flood their stores with a lot of people. I think once everybody got a little more comfortable with the environment, the push became a little more normalized in May and June. And then the fourth quarter has been, like I said, up 40%.

So some of this has been COVID-related, but I think a lot of the people who have joined the category, we have a lot of reasons to believe that they'll remain in the category and be sticky. About 30% of our consumers who are engaged in edible gardening this year were new consumers or lapsed users from recent years.

And in the lawns category, we believe there's about 8 million new users this year. So our belief is once people join the category, it helps them with their mental and physical health. They've made an investment. They're happy with how it goes. Even if they were to go back to work at a more normalized level, and I doubt the whole world goes back to 5 days a week in the office. But we think people will continue to engage in our category, and we have a lot of reasons to believe that, that's going to continue on.

And then switching over to Hawthorne, we expect to have a really terrific year this year. We'd started out planning for mid-teens externally, but had internal expectations to do better. We, certainly, didn't see 60% growth. But again, I think we benefited a bit from people staying at home, engaging in the category. We've taken a tremendous amount of market share. And again, I think once those consumer behaviors take hold, I'd be surprised if we really give anything back going forward. So time will tell, but we have a lot of optimism by Q1. We feel good all the way through the first half of the year. And then I think we'll have to reassess, but we have a lot of good reasons to believe.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

You mentioned that of old gardening. I'm curious how big that is of a business for you right now. And what's driving that? Is it people concerned about the food supply? Or they just want the freshest vegetables, for example?

Thomas Randal Coleman
Executive VP & CFO

Yes. Sorry, Joe, I'm trying to get my video on. It's so hard do that.

James D. King
Chief Communications Officer, Executive VP & President of The Scotts Miracle-Gro Foundation

And so -- I'll jump in a little bit here at the beginning, and then Randy can add some color. So edible gardening has been the fastest-growing segment of lawn and garden in general for the last several years, particularly popular with new homeowners, millennial homeowners. They index really strongly in this space. So we've been seeing a lot of momentum in that space for some time, which is why several years ago, we took a minority interest in Bonnie Plants, which is the largest provider of edible plants, live goods in the retail space today.

So this year, we just saw more of that momentum picking up. And we saw it early in the spring. And actually, it continued all-season long. You saw people planting vegetable gardens well into the summer, normally way later than they -- or way later than they typically do. So a lot of momentum as a result of that. That helped, not just our investment in Bonnie, but our growing media business. Our soils business this year is up well over 40%. And we've been seeing in that space, in particular, as quickly as we could get products manufactured and through our line, we're getting them on the truck and getting them to retail, and they're getting taken off the shelf. So that's where the real demand has been.

I think part of our plan going forward, to keep those people engaged, is to kind of build a relationship with them based on the successes that they had as gardeners this year. So you're seeing a lot of communication these days from the Miracle-Gro brands, talking to people about their harvest, what to do with their harvest, how to freeze it, how to yard, how to cook with it, maybe what to do with surplus. And I think you're going to see that brand, in particular, work really hard through the off-season to remind people of the benefits of edible gardening, and why they got in the category to begin with, and hopefully bring them back in next year. So we're really bullish on that part of the segment.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

And how big is that business for you, Jim?

James D. King
Chief Communications Officer, Executive VP & President of The Scotts Miracle-Gro Foundation

So the buying business is more than a $300 million business. Those sales don't run through our P&L. And then our growing media business is well in excess of $650 million now, and a big part of that is dedicated to edible gardening.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Okay. Now normally, we'll been talking about the weather, right? And that would be the difference between, let's say, U.S. consumer up 1 versus U.S. consumer up 3. Clearly, we've had other factors this year to overwhelm that. But just curious, has weather been a positive or a negative, generally speaking?

James D. King
Chief Communications Officer, Executive VP & President of The Scotts Miracle-Gro Foundation

I think it's probably been fairly -- if you -- I think the way that we tend to look at it is that weather tends to normalize itself over the course of the year, Joe. And there's nothing in any over the entire country, that's probably true again this year. I think, in the Northeast, again, in particular this year, weather caused us to get off to a slightly slower start, but then came back really nicely. So I don't think weather has been necessarily a tailwind, but I don't think it's been much more than neutral on a total company basis over the course of the year.

Thomas Randal Coleman
Executive VP & CFO

And Joe, to add a little more color to that. If you look at our sales by region, and we break our business down into the West, the South, the Midwest and the Northeast, everyone is circling around 25%, give or take a point. And that's on a year-to-date basis. When we look at results every month and every week, they're also very, very tight. So I really don't think anything going on this year is really related to weather. It's more just about national engagement and then lawn and gardens. People have spent more time at home, and learned to enjoy working out in the yard.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

You mentioned earlier, the $8 million-or-so roughly new lawns customers this year that entered the category. I guess 2 questions there. First, why weren't they in the category to begin with? And two, maybe more importantly, how do you keep them in the category next year?

Thomas Randal Coleman
Executive VP & CFO

As far as why they were not, some are lapsed users. When we look at our business, the most important consumers we have are the ones that -- what we call the weekend warriors, that year in, year out, are going to show up. And if it does rain on 1 week, they're going to come back the next week. They're going to plant their garden every year. They're going to take care of their yard. And that's really the bread and butter for our business.

I think over time, as we look at what's happened in about the last 10 years, we have seen a decline in units in our lawns business, I think, just because people a little more focused on other things. I think they get consumed with their telephones and their devices rather than being on the yard. And I think we've been able to see a shift back towards people wanting to be outside and get out of their homes as it works from home.

So again, I think we're encouraged about what that's going to look like. And we're using things like Bonnie Plants, that Jim mentioned, to stay engaged with consumers all year long. It's really encouraging to me to see that the retailer is gearing up for a big fall, and we're going to continue to market for those same people all the way through the winter.

And when you can see in our 40% growth rates in months like July and August when it's hot outside, and I'm not just talking about Ohio or New York, I'm talking about Arizona and Florida and the South is still up 40%. To me, that's a really encouraging sign.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

So if we look forward to next year, and I think, Randy, you touched on this a little bit in your prepared remarks. Hopefully, we're not in the same situation from a COVID standpoint. People are able to get out and about and go on vacations and play travel sports and go to camps and things like that.

So could we talk about how you will lap this year next year? I mean obviously, again, you're probably not going to see the POS numbers that you've seen in a post-[Father's Day], let's call it, next year. So how should we think about your ability to anniversary this? What is largely COVID-driven relative to 2020?

Thomas Randal Coleman
Executive VP & CFO

Right. So I would expect the momentum we have right now to continue. It's been a bit of a frustration for us internally, and that we did expect things to slow down once we got past mid-June. And clearly, it hasn't. So at this point, I don't see any reason to think it will slow down, even if there were a vaccine tomorrow. And if that were the case, I'd still think people will want to find the right balance between working from home and working from the office. And again, when they're working from home, they look out the window, like I am right now, and they want to make sure that the yard looks nice and it's enjoyable for their family.

So that's the largest thing. Again, our marketing focus has changed quite a bit from -- historically, the great majority of our advertising would be on TV. And we've really engaged much more on social media with different agencies this year, and talking to consumers directly, practically all the time, and we continue to do that all the way through the winter with what we call our 365 marketing campaign now.

The retailers are going to be, I believe, a lot more competitive and a lot more promotional, especially in March, April and May versus what we saw this year. And I think e-commerce, not just in 2021, but beyond that, is really going to take hold and be a bigger part of our business. So whether we're talking about our own websites, whether we're talking about e-commerce more broadly, or whether we're talking about our largest customers and their buying online and pick up curbside initiatives, I think we're best positioned from national brands and national infrastructure and service to be able to fulfill all the needs related to that.

So -- and then the final thing is, we've been trying to build inventory in the fourth quarter. We haven't really been able to and expect in the year about flat in our own inventory, but we're going to have plenty of inventory in our barns in the front part of next year to make sure that we're not missing out. And then we'll have to reassess about halfway through the year and see where we are. But a lot of optimism, especially for the first half. And then I think we're doing all the right things that make those consumers sticky beyond that.

James D. King
Chief Communications Officer, Executive VP & President of The Scotts Miracle-Gro Foundation

Joe, if I can just elaborate on the marketing piece a bit. Randy mentioned what we're doing with digital. I think it's important for people to understand that this is way more complex than simply buying ads on Facebook or buying ads on Instagram or banner ads on websites.

So part of what we've really been working on is understanding the demographics of who've been -- who's been buying and engaging in the products this year, what platforms they're using, what demographically they look like, where they shop, where they live, whether do they have kids, understanding that the creative that may appeal to me may not appeal to you. The creative that appeals to you probably doesn't appeal to your wife.

So moving away from kind of a simple approach where handful of pieces of creative are what we use to drive activation and moving towards a place where literally, we're talking about tens of thousands of pieces of creative that change every day, really kind of understanding what's happening real-time with these consumers so that we can talk to them in relevant ways and keep them engaged. So it's a very, very different approach. And anything that we have done. It's been working extraordinarily well with us. We'll be working more closely with our retailers going forward as well. And we've seen a lot of success in using that sort of activation to also drive specific foot -- specific consumers and specific retailers for specific product promotions.

So a lot of reasons to be really bullish about the marketing approach that we've taken. And I think it's just important for people to understand exactly what we're talking about.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Is that an internal initiative for you, Jim? Or have you partnered with an outside [party]?

James D. King
Chief Communications Officer, Executive VP & President of The Scotts Miracle-Gro Foundation

We've been partnering with an outside firm, people who are kind of social media users may know the name, Gary Vaynerchuk. Gary has been working very closely with us. His firm, VaynerMedia, has been working pretty side-by-side with us for a couple of years. We've really ramped up our efforts with Gary and Nick and that team this year. We're going to go further next year.

And over time, Joe, I think the goal here is to build more of an internal skill set as well. But certainly, the learnings from Gary and his team have been really helpful to us over the last 2 seasons this year, in particular.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

And you mentioned earlier that pricing probably added 1 point, let's call it, to U.S. consumer sales this year. Is pricing going to be a part of the equation as well next year?

Thomas Randal Coleman
Executive VP & CFO

What is a point for our U.S. business and probably a little bit more than that this year for Hawthorne as well. Looking forward to next year, there will be some pricing in our P&L. Exactly how much? We're still in the process of determining. And we typically kick off-line our dues April, May, and we finalized them September, October. So we'll have answers by November 4 on -- and we can be a lot more specific about pricing, but there will be pricing in our P&L next year.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Okay. One of the things that you guys have benefited from this year is a lack of promotion for [Hawthorne], which is that you and your retail partners really didn't have to do much of it. How do you see the promotion environment playing out next year?

It sounds like we're going to see a bit of an uptick on that next year, but probably not back to what we were, let's call it, in 2019. And what's the impact on the P&L? Could that offset the price increases you guys have planned or probably not that big?

Thomas Randal Coleman
Executive VP & CFO

Yes. So we increased our investment in the P&L and SG&A across the board, especially media this year. We plan to do more of the same next year. So we'll still be aggressive. Don't necessarily tie it to pricing, we're doing it regardless. But we'll keep pushing things. As far as where I'd see it, the biggest increase, though, is really from retailers. So this year, they did pull back a lot. And again, I don't see them going back to what they would have done before 2020, but probably somewhere in the middle, probably more competitive, more promotional, and I think we'll benefit from that, but that won't be impacting our own P&L.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Okay. And then sticking with '21, what are the puts and takes do you see on the gross margin line? Thinking, in particular, commodity costs, for example, or freight costs? I know you guys do a very good job of trying to hedge as much of those commodity costs as you can. But I'm curious on what we should expect next year on that gross margin line.

Thomas Randal Coleman
Executive VP & CFO

Sure. So our typical approach that we employ again this year is to hedge our biggest commodities, being urea, diesel and resin, and we're about 2/3 hedged as we start out the year. So we have a lot of cost predictability.

And the one area that we're watching a little bit that we can't really plan ahead on as well is on spot market rates around trade in March, April, May, when we really start to do start shipping. So time will tell. But I think the commodity environment is flat to maybe a little bit of a headwind, looking head into 2021, but not in a big impact.

This year in 2020, our gross margin rate will probably be somewhere around flat, which is a little bit of a misleading story in that we've improved our margin rate, both in the U.S. and Hawthorne. It's just a dramatic growth in Hawthorne being at a lower margin rate has brought the weighted average down. So I'd expect, again, too soon to provide guidance, but a similar kind of phenomena next year in that I think expect Hawthorne to grow faster than our U.S. core since Hawthorne is slightly more lower margin rates. There will be a mix impact to that. But I think within each business, mix should be positive. The combined environment shouldn't be very impactful, and I do expect pricing to be a little bit of a benefit next year.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

And what about chatter? And obviously, this year, your DIY Partners had a fantastic year. So I'm curious if we do see a little bit of -- a little bit more growth next year in independents and hardware? Do you see that impacting margin that dramatically?

Thomas Randal Coleman
Executive VP & CFO

Well, what we have seen this year is when the home centers were a bit reluctant to bring a lot of consumers into their stores back in that March, April, May time period, that I think there was a bit of a share shift from big box stores to smaller hardware independents, and even clubs. And I think the big boxes become more competitive in the last 3 or 4 months. And I know that they're planning to be more competitive next year as well. So time will tell.

As far as margins by customer, they're all fairly equitable. So there's not a big mix story there from one customer to the next.

James D. King
Chief Communications Officer, Executive VP & President of The Scotts Miracle-Gro Foundation

And Joe, one of the -- we feel good about next year, especially at the break of the season. So you mentioned the strength of the home centers. A lot of that's happened since kind of Memorial Day on.

Our season breaks earlier than that. And so if you look at April, which is a really critical month for us, and early May, you would have actually seen a lot of pressure on home centers because, to Randy's point, they couldn't drive foot traffic into their stores and at the most critical time of the year.

So our expectation is they're going to work really hard at the break of the season next year to claw that foot traffic back, get that market share back. At the same time, some of the retailers that they lost that market share, too, are going to try equally hard to keep it. So the retail dynamic for us at the break of the season next year should be really beneficial.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Okay. That's helpful. Shifting to the online strategy. Online has never been a big part of your business. I would imagine you've seen an uptick this year. You've talked about that in the past. When you think about -- or talk about how we should think about growth in that channel going forward, is this something that you're focused on?

Thomas Randal Coleman
Executive VP & CFO

It definitely is. And our biggest e-commerce business is what we sell-through our big box stores, it's buy online, pickup in store, where I think we have a big advantage in that we have national brands with national scope and if someone is in Washington State or if someone is in Florida, and they are shopping for product, we have those national brands that they can buy. And we'll have the service and we'll have the product in the store.

So I think that's actually -- if you look across where our share is the greatest, we actually over-indexed in curbside pickup versus people buying in the stores or even buying online. But also our e-commerce business has grown dramatically well with our own websites this year. So it was just a few million dollars last year, it was probably approaching $25 million this year. And we've learned a lot. We haven't made a lot of money, but it's an area that, going forward, you'd think that we would be able to do well and to improve on. And that's going to be an area we are investing money, even here in Q4, to try to get ahead of things and build the infrastructure so we can do that better.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

And are there products that do better online, let's say, than you might think from a product standpoint?

James D. King
Chief Communications Officer, Executive VP & President of The Scotts Miracle-Gro Foundation

Right. I think not everything works online, Joe, but listen, like, we've even been able to sell fertilizer online this year. A lot of that being sold through a subscription model. So I think the things that don't work as well are going to be things like soil and mulch, where people don't usually buy a single bag. They'd buy 5 bags of soil or 20 bags of mulch. That's a harder problem to solve. But while some products work better than others, I think we've had success across all -- most all product categories this year this way.

Thomas Randal Coleman
Executive VP & CFO

Joe, we've also built some digitally native brands that you might not be nearly as recognizable as Scotts Miracle-Gro, but really intended just to build that relationship with consumers. So Lunarly is one. I'll plug that one. And we also have a brand called Barkyard that's intended for lawn care consumers who also have dogs and the challenges that they face. So these are things that we just saw in our own websites that right now would not be sold through retailers, but we think it's an interesting part of our business, and it's a good way to build that connection with consumers.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Got it. Okay. So if we go back to your last earnings call, and I think Randy, you touched on this as well earlier, you mentioned that while not giving guidance, you could see another year of double-digit EPS growth next year, even if the U.S. consumer business is flat. And a big reason for that, I think, is some favorable trends that you guys are seeing on the SG&A line.

Could you lay out those for us, maybe quantify the impact? I think you mentioned it's about $1 a share. So if I just do the math here, regarding the $7.25 this year, all else being equal, we're looking at an EPS number well into the $8 level next year.

Thomas Randal Coleman
Executive VP & CFO

The biggest piece behind that dollar per share number that we've talked about is around variable compensation, both short-term and long term. So annual bonuses will be maxed out this year, plus the Board has employed some discretion. So we're also providing bonuses to people that typically want to receive them, hourly associates in addition to that. And then some of our long-term plans, given how terrific our results have been this year, we've topped off some of those plans as well.

So returning to more normalized levels next year, you get a nice tailwind from that. And we've also been as aggressive as possible while trying to pull some spending into the fourth quarter and get ahead on things like D2C and R&D and IT investments, some media and marketing, our fourth quarter will be higher than a year ago. Things that we can do because we are the -- not just the capability, but also the opportunity to try to get ahead of some things.

So if we have another fantastic year next year, those might anniversary next fourth quarter, but they don't necessarily need to. So we've been able to get ahead of things.

So collectively, that's worth about $1 per share benefit to next year, again, assuming that total company sales are about flat. So we feel optimistic about next year's bottom line at this point.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Is there anything that's -- that could offset that potentially, beyond the obvious tough comparison, weather, what have you?

Thomas Randal Coleman
Executive VP & CFO

Not necessarily. Like we talked about the commodity environment being fairly benign. I think the question will come down to what do the second half sales look like for both businesses, but especially the U.S., but for all the reasons we've talked about, we're really encouraged about making our new consumers sticky and being able to not grow 40% off next -- up this year is 40%, but being able to anniversary that more or less. That's what we're targeting to do. And if we do that, we should have a really successful year again next year.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Okay. So in terms of Hawthorne, you mentioned earlier, your outlook coming into this year, I think, was for sales growth of 12% to 15%. I think internally, you had expected a little bit better than that. I'm not sure 60% growth was what you had in mind, but that looks like where we are today.

So -- and it sounds like a lot of that is states opening up. I imagine people working from home. There's probably more use. So maybe talk about what you're seeing, from a cannabis demand standpoint, are there more cannabis users? Are they using more cannabis? Or from -- in terms of existing users, what's been driving that super growth, number one?

And number two, I would think that there's some relationship between your growth and the growth of cannabis demand, at least over the medium to longer term. Is that the case? And when do you see that sort of to moderate toward that, let's call it, high single digit, low double-digit growth?

Thomas Randal Coleman
Executive VP & CFO

Right. So at the core, what we really tried to predict over time is looking at consumer demand. Now that will increase, which we think will be high single digits, and we've used that based on data that we've seen historically. Colorado being the place that has probably the best data that was really the basis for our long-term model.

But what we've seen is Colorado, again, as an example, pre-legalization of cannabis the per capita usage rate was low double digits, call it, 10%, 11%, 12% is now nearly 20%. So even if you look at other states that are starting at a much lower base, if you see similar levels of increase, that certainly helps. But when you think about it even more broadly, when a state does become legal, the 2 years before product is actually sold, there's a big capital investment that we benefit from. First couple of years after legalization, continue to see really good results. Eventually, things normalize in over a 5-, 6-, 7-year period, get down to more of in the single-digit kind of growth profile.

But as we see that roll out, year-over-year, we look at new states that are on the horizon and perhaps imminent. I think that's a positive for us. And also, the products that we sell are really focused on indoor growing, which everything east of Colorado is going to be in these states that flip indoor growing. So all those tailwinds, we think are a positive for us and give us a lot of reason for optimism.

Joseph Nicholas Altobello

Raymond James & Associates, Inc., Research Division

Is there a relationship both longer-term between cannabis demand growth and your growth?

Thomas Randal Coleman
Executive VP & CFO

For sure. So that's -- as we try to predict what's going on, you can get supply and demand imbalances like we saw back in late 2017 that created an issue for us in 2018, but we don't see anything like that happening again. That was California, which remains almost half of our sales. We think that has worked itself out. We're very aware of what wholesale and retail prices are in the marketplace now, and they seem stable.

So at this point, we don't see any kind of misbalance between supply and demand. And we know our retailers don't have the physical capacity to load products. So what we're selling in is being passed on and being consumed and makes us feel good about the stability and sustainability of our business right now.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

And what does the competitive landscape look like in that industry? I know there's -- it's been evolving, shall we say, over time. So I'm curious, have you seen new entrants? Are you more worried about existing players or new players coming into that space?

Thomas Randal Coleman
Executive VP & CFO

We haven't seen new players, but our largest competitor is another distributor that -- it's not public information, and we don't have any special insights, but our expectations are that they're doing about the same level of sales as they would have been 2 or 3 years ago. And we've gone from a business that started with general hydroponics. That was about $130 million investment. We've now invested in $1 billion. And we're going to have $1 billion of sales this year.

So I think we're clearly taking market share from that company. The number third distributor in the marketplace went out of business a couple of years ago, and I'm certain that we picked up a lot of market share from them as well. So it's difficult to quantify because we don't have the same level of granular data as we do with our consumer business, but I'm confident in saying that we've taken a lot of market share this year.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

And last question is because we've got about a minute left, but in terms of capital allocation, your balance sheet, obviously, is in a much better place than it was a year ago, let's call it, you probably end this year well under 3x levered. What are your priorities in terms of capital allocation? And do you see another special dividend down on the horizon? Would you anticipate a step up in buybacks this year?

Thomas Randal Coleman
Executive VP & CFO

So we'll certainly maintain and continue to increase our annual dividend. We increased that 6% or 7% going forward. Like you mentioned, we did a special -- we'll probably have increased internal uses of capital, just trying to get ahead on supply chain and some infrastructure build, both for the U.S. and Hawthorne. So our typical CapEx rate is in the $75 million-or-so range. We'll probably be over $100 million in 2021.

So we're in a great place. Lots of flexibility. Lots of optionality. If there's a good acquisition at the right price, with the right fit, we're glad to do that all day long. There's nothing imminent at this point that we'd say it's definite demand on our capital, but we're in a good place to be. And whether it be share repurchases or another special, if the year goes as well as we plan, we'll likely be doing one or both of those as we start working into 2021.

Joseph Nicholas Altobello
Raymond James & Associates, Inc., Research Division

Well, great. It looks like we are just about out of time. So with that, I did want to thank Randy and Jim once again for your time. And I hope everyone has the great rest of their day. Thanks for joining us.

James D. King
Chief Communications Officer, Executive VP & President of The Scotts Miracle-Gro Foundation

Thanks, Joe.

Thomas Randal Coleman
Executive VP & CFO
Thanks. Thanks, Joe.