

Holley Inc.
2Q 2025 Earnings Conference Call
August 6, 2025

Presenters

Anthony Rozmus, Investor Relations
Matthew Stevenson, President, CEO
Jesse Weaver, CFO

Q&A Participants

Brian McNamara - Canaccord Genuity
Christian Carlino - JPMorgan
Martin - Raymond James
Phillip Blee - William Blair
Patrick Buckley - Jefferies
Michael Baker - D.A. Davidson
Joe Feldman - Telsey Advisory Group

Operator

Good morning, ladies and gentlemen, and welcome to the conference call to discuss Holley's Second Quarter 2025 Earnings Results. At this time, all participants are in a listen-only mode. Later, we will conduct a question and answer session and the instructions for asking questions will be provided at that time. We ask that participants limit themselves to one question and one related follow-up during the Q&A period.

Please be advised that reproduction of this call in whole or in part is not permitted without written authorization of Holley. And as a reminder, this call is being recorded and will be made available for future playback. I would now like to introduce your host for today's call, Anthony Rozmus with Investor Relations. Please go ahead.

Anthony Rozmus

Good morning, and welcome to Holley's Second Quarter 2025 Earnings Conference Call. On the call with me today are President and Chief Executive Officer, Matthew Stevenson, and Chief Financial Officer, Jesse Weaver.

This webcast and presentation materials, including non-GAAP reconciliations, are available on our Investor Relations website. Our discussion today includes forward-looking statements that are based on our best view of the world and our businesses as we see them today and are subject to risks and uncertainties, including the ones described in our SEC filings.

This morning, we will review our financial results for the second quarter of 2025 and discuss guidance for full year 2025. At the conclusion of the prepared remarks, we will open the line up for questions.

With that, I'll turn the call over to our CEO, Matthew Stevenson.

Matthew Stevenson

Thank you, Anthony, and good morning, everyone. As we look back on our second quarter of 2025, I am happy to report that the momentum we began building more than 24 months ago continues to grow. It's been a highly productive quarter, one that not only reflects strong operational discipline, but also the impact of staying focused on our strategic priorities. Thank you, as always, for your continued support as we navigate a constantly evolving consumer and macroeconomic environment.

For the second straight quarter, our core business delivered solid growth. Just as a quick reminder, when we say core business, we're referring to results that exclude the businesses we divested in the product lines we phased out as part of last year's strategic rationalization efforts. This quarter, our team made strong progress across the board with core growth showing up in every division of the company. What's especially encouraging is that we're again seeing this momentum in both our direct-to-consumer and business-to-business channels. That speaks to the strength and balance of our omnichannel strategy.

As we emphasized many times before, our omnichannel approach is a cornerstone of our growth strategy as the leading consumer enthusiast platform in automotive performance aftermarket. We're committed to meeting customers wherever they choose to do business, whether it's through e-tailers, distributors, wholesalers, third-party marketplaces, installers, national retailers or our own e-commerce platform.

Our second quarter performance reflects the foundation we have built over the last two years in key areas like go-to-market execution, product innovation, digital capability and operational excellence, all of which are now driving the progress we're making under our three-year strategic plan. With that foundation firmly in place, we're focused on keeping up the momentum and building on the progress we've already made.

Before we get into the specifics of Q2 performance, I want to revisit something we discussed last quarter, and that's tariffs. I'm proud to say that the tariff mitigation plan we introduced in Q1 is working, thanks to the incredible effort and execution from teams across the company. This wasn't luck. It was a result of careful planning, strong cross-functional teamwork and consistent hard work. From the initiatives we developed to lower our tariff exposure across the supply chain to the pricing strategies we rolled out this past spring, all that has come together to form a smart, resilient response. Because of these efforts, we're currently not forecasting any meaningful impact to free cash flow or margins this year or next. This is a great example of

how strong leadership, operational focus and a culture of accountability can overcome major challenges and deliver real results.

Now let's turn to Slide 5, which includes our highlights for the second quarter of 2025. We continue to build momentum in Q2, delivering a solid 3.9% revenue growth in our core business across all divisions. This performance reflects consistent execution of our strategy and the resilience of our operating model. Most notably, we achieved free cash flow of \$35.7 million, marking the highest quarterly free cash flow generated in our history. This is a clear testament to both our disciplined capital management and the strong cash-generating power of the business. We continue to execute against our strategic framework, which drove approximately \$27 million of revenue from key initiatives this quarter. This includes focused work streams across our commercial and operational pillars that are accelerating profitable growth.

Our growth remained broad-based with expansion across more than 20 of our brands in both the direct-to-consumer and business-to-business channels. In the B2B channel, we further strengthened our relationships with key partners, driving approximately 6.5% growth in the channel. This growth stems from increased sales support, deeper integration with our partners and a relentless focus on customer satisfaction. In direct-to-consumer, we saw an increase of 8.6% overall with especially strong performance on third-party marketplaces like Amazon and eBay, which grew over 28%. These platforms continue to be a major growth lever for us as we meet customers where they prefer to shop.

Product innovation remains a cornerstone of our performance. Combined with strategic pricing initiatives, our efforts contributed \$10.8 million in incremental revenue this quarter. We continue to calibrate pricing to match customer value perception while ensuring competitiveness and profitability across all channels. Lastly, as I mentioned, we made significant strides in our supply chain initiatives, which are forecasted to effectively offset tariff-related pressures and help preserve margin stability. These efforts underscore our proactive approach to tackling issues head on and getting in front of them before they impact the business.

Let's turn to Slide 6, which features some more quantitative highlights from the second quarter of 2025. We achieved net sales of \$166.7 million, reflecting a 3.9% increase in the core business compared to the prior year. This solid growth continues to validate the strength of our strategic execution and the dedication of our teams across all divisions. Our gross margins were 41.7%, up 26 basis points year-over-year, demonstrating continued stability and positive momentum even in the face of external cost pressures.

The improvement is partially due to strategic product and pricing actions as well as operational initiatives, including supply chain efficiency. Free cash flow, as I mentioned, reached \$35.7 million, an increase of \$11.3 million versus the prior year. This strong cash generation highlights the underlying strength of the business, aided by disciplined capital allocation and working capital management.

Adjusted EBITDA margin came in at 21.9%, down 74 basis points year-over-year. This decline reflects the normalization following prior year SKU rationalizations and divestitures, but it remains well within expectations given the shift in product mix and ongoing investments in innovation and growth.

Regarding new product activity in Q2, we introduced several launches across our portfolio, and I'd like to highlight just a few standout examples. We launched the Terminator X Bluetooth module, enabling wireless engine tuning via a smartphone. It's quickly gaining traction with strong early demand, enhancing our EFI platform and driving mobile integrated growth. We also expanded our Arizona Desert Shocks Mesa 2.5 line by adding new applications to meet growing demand in the off-road market. These premium shocks deliver exceptional performance and durability, positioning ADS for continued growth with enthusiasts seeking race-proven technology for everyday builds.

In our Euro segment, our APR brand introduced new high-performance exhaust systems for the Audi S4 and S5 platforms. These upgrades deliver improved sound, reduced back pressure and weight savings, broadening our appeal in the premium European space. Additionally, we released new colorways for the Simpson Outlaw Bandit 3.0 motorcycle helmet, building on this popularity of this iconic model. The refreshed designs inject energy into a top-performing product and further strengthen our position in motorcycle safety. Together, these launches highlight a small example of our continued focus on innovation, consumer engagement and expanding our leadership across key enthusiast categories.

On the operational metrics, we also delivered significant progress in the quarter. We achieved a 2.2% year-over-year increase in the in-stock rates for our top 2,500 products, a \$1 million improvement in operational efficiency and a 17% year-over-year reduction in past dues. Additionally, we've reduced inventory by approximately \$9 million since the beginning of the year, contributing meaningfully to improved cash flow and working capital efficiency.

On the marketing front, our focused promotional efforts continue to drive results. We recorded an 8.6% year-over-year increase in D2C sales, bolstered by third-party platform growth of more than 28%. Our earned media impressions reached 463 million from 657 media clips, and our social media following grew 2% over the previous year, reflecting deeper engagement with our enthusiast customer base.

In summary, our second quarter performance demonstrates continued execution of our strategic priorities, driving growth, operational excellence and shareholder value creation across every part of the organization.

Let's take a closer look at some of the standout core business growth we saw across our divisions in Q2, shown on Slide 7. In the domestic muscle vertical, we delivered 6% year-over-year growth, driven by sustained consumer demand and the enduring strength of our brands.

Many brands within this division posted high single-digit growth in our core product categories, highlighting solid performance across the board. Our Modern Truck and Off-Road division led the way with an impressive 17% growth. This was fueled by standout results from several of our priority brands, including at least five of our power brands that recorded double-digit growth in their core businesses. The Euro and Import division experienced strong momentum as well, up 4%. Now the Euro brands, of Dinan and APR within this were up 20% combined. However, this growth was offset by year-over-year revenue timing shifts in our import division, which moderated overall performance in this vertical.

The Safety and Racing division reported 1% growth, but that figure doesn't fully reflect what's happening under the surface. Our Simpson and RaceQuip brands posted a combined 15% growth. Plus, the division is currently navigating a regulatory transition known as the Snell cycle, which happens every five years and impacts automotive motorsport helmets. Distributors are limiting orders until the next certification SA 2025 helmets become available to enthusiasts in October. As a result, we anticipate a significant rebound in growth in the second half of the year.

Overall, these results affirm the strength and the resilience of our core business. Our strategic focus on investing in power brands, streamlining accountability and aligning resources is driving measurable success. Despite a challenging market environment, our commitment to brand leadership and disciplined execution continues to deliver sustainable core growth across our major divisions.

On Slide 8, we revisit the eight areas that form the foundation of our strategic framework, which we have reviewed in prior calls. At the center of this framework lie our steering principles. The first of these principles is fueling our teammates, which supports our ambition to establish Holley as a recognized Great Place to Work. Our focus remains on fostering a workplace where team members feel empowered, have meaningful opportunities for advancement and look forward to being part of a dynamic and inclusive environment.

Our second principle is supercharging our customer relationships, whether that's with our passionate consumers or our trusted B2B collaborators. This principle touches three vital components of the framework: building and delivering the premier consumer journey in our industry, becoming a trailblazing trusted partner to our B2B customers by finding innovative paths for shared growth and bringing to market innovative new products that set the benchmark in their categories. We support these priorities by deliberately managing and merchandising our entire portfolio with clear differentiation.

The third and final principle, accelerating profitable growth focuses on strategic expansion into new global and adjacent markets, pursuing transformational M&A and enabling reinvestment through continuous operational improvements. Together with the other initiatives, these actions drive us toward our overarching aim, delivering superior financial results.

Now on to Slide 9. I'm pleased to share the highlights and the achievements for the second quarter as captured in our updated strategic initiative tracker. Under our Trailblazer and trusted partner pillar, encompassing our B2B efforts, we've seen another quarter of strong performance. Revenue from our top 50-plus accounts accelerated significantly, contributing \$8.3 million in growth. Our Holley Pro small customer initiative also continued to gain momentum, adding \$1.8 million in revenue, thanks to our focused sales team, proactive outreach and deepened customer relationships. In total, these B2B sales initiatives contributed \$13.2 million in incremental revenue in Q2.

Turning to our premier consumer journey pillar. Our e-commerce strategy remains a key driver of growth. Year-to-date, e-commerce revenue is up approximately \$4 million. Our efforts on third-party platforms, especially Amazon, has been particularly successful with over 50% growth in Amazon sales and over 40% growth across all 3P platforms in the first half. These efforts alone added \$2.2 million in incremental revenue during the second quarter.

Innovation continues to be a cornerstone of our growth. We launched new products across all 4 divisions, delivering approximately \$8 million in revenue. At the same time, our portfolio management strategies, including strategic pricing and optimization of our active portfolio generated an additional \$3 million in B2B sales. In total, this pillar added \$11 million to our top line in Q2.

Our international expansion efforts remain on track. The progress in Mexico has validated our product market fit and our go-to-market strategy, setting a solid foundation for future growth. Additionally, we expanded our reach in the car dealer channel with six more BMW dealers joining the Dinan program, bringing the total to 28 participating dealers. These combined initiatives while still early in their adoption, generated \$1.1 million in revenue for the quarter. We continue to make strong progress under our Fund the Growth pillar. In Q2 alone, we completed and implemented over \$2.5 million of purchase savings projects and achieved more than \$1 million in operational improvements. Together, these efforts resulted in \$3.5 million in cost savings for the quarter.

We're also proud of the ongoing progress we're making in strengthening our culture and employee engagement. As reported last quarter, we saw a 3% increase in our Great Place to Work Pulse survey scores, an encouraging sign of our efforts taking root. Looking ahead, we're excited to build on this momentum with our annual employee survey scheduled for later this fall. Additionally, through continued operational efficiencies, we remain on track to achieve our year-end target for revenue per employee. All told, we generated \$27 million in revenue from key strategic initiatives and achieved \$3.5 million in cost savings. In addition to advancing our strategic initiatives, we have continued to prioritize actions to mitigate the impacts of tariffs introduced since our last meeting.

As we promised during our last earnings call that we would come back to you during this August call and provide greater clarity to the impact of tariffs to our business, both in 2025 and 2026. Today, we are going to do that. Let's walk through some more detail first on Slide 10.

During last quarter's call, we outlined our detailed comprehensive plan to tackle tariffs, an effort we had already been driving through a swiftly established cross-functional project management office. To address the various aspects of tariff mitigation, we organized the work into five major work streams; governance, products, logistics and supply chain, regulatory and classifications and pricing and margin protection. Our approach was multifaceted, supported by daily meetings to maintain momentum, track progress and ensure alignment across teams. Each work stream was intentionally structured to address a distinct set of challenges and opportunities, enabling a coordinated and effective response.

As we highlighted, the product work stream was a particularly critical component of our overall strategy. It kicked off approximately 120 days ago with an ideation workshop involving 11 product teams, each led by dedicated team leaders. The workshop focused on identifying and prioritizing high-impact initiatives and building a consistent executable playbook. That playbook included supplier negotiations, relocations, resourcing decisions, footprint analysis and make versus buy evaluations.

In addition, we verified product classifications to ensure compliance and to optimize how our products are coded. The collective focus, coordination and tenacity across all teams have led to meaningful results, which I'll walk through next on Slide 11.

Through a combination of strategic negotiations with existing suppliers, targeted relocations, sourcing from new partners in lower-cost regions and selective in-sourcing, we've executed on over \$15 million in tariff mitigation opportunities through 2026. While disciplined execution will continue to be essential, we're confident in our strategy, our team's capabilities and our ability to successfully navigate this evolving landscape.

In short, our response to the tariff environment has been both proactive and comprehensive. We launched dedicated work streams, facilitated cross-functional workshops, secure optimized logistics solutions, brought in leading regulatory experts and executed targeted pricing actions, all aimed at minimizing the financial impact of tariffs on our business.

That said, we all understand that the tariff landscape remains highly fluid. However, based on the progress of our current mitigation efforts and pricing strategies, we are not projecting any adverse impact to free cash flow or margins in 2025 or 2026. With that, I'll now turn things over to Jesse, who will walk us through a detailed financial analysis and year-over-year comparison of our Q2 2025 performance, followed by a deeper look into the projected impact of our tariff mitigation strategy. Jesse?

Jesse Weaver

Thank you, Matt, and good morning, everyone. I'd like to start by providing an update on our progress against our financial priorities, then discuss our second quarter 2025 results, our updated view on the tariff impacts to free cash flow and our refinements to our guidance.

Moving to Slide 13. We remain focused on our financial priorities, which are restoring historical profitability and optimizing working capital. Our keen focus on these financial priorities has allowed us to generate our strongest quarterly free cash flow results in the history of Holley, achieving approximately \$35.7 million in Q2. We relentlessly work towards restoring historical profitability and make progress towards our full year operational efficiency targets again in the second quarter. We saved roughly an additional \$1 million in the second quarter, primarily driven by a reduction in freight costs, which brought our year-to-date cost savings in 2025 to just over \$2 million. And as a reminder, we anticipate savings of \$5 million to \$10 million through improved manufacturing efficiency, warranty and return policy compliance and quality improvements to better the customer experience in 2025.

In Q2, we made strong progress optimizing working capital by proactively managing inventory, by continuing to make improvements in our SIOP processes to build a more agile demand-driven model. These efforts are aligning production with market needs, optimizing safety stock and lead times and cutting slow-moving inventory, all while maintaining high service levels and boosting operational efficiencies. Through these efforts, we've been able to reduce inventory by more than \$9 million year-to-date and are on track to achieve our year-end reduction target of \$10 million to \$15 million.

On Slide 14, we'll walk through our key financial metrics for the second quarter. Net sales for the second quarter were \$166.7 million versus \$169.5 million in the same period a year ago. The decrease was primarily related to lower sales volume, partially offset by improved price realization. Excluding approximately \$9 million of divestiture and strategic product rationalization sales from net sales for the second quarter of 2024, we achieved growth of roughly 3.9%, exceeding our expectations for the quarter.

Core business growth once again came across all divisions and is a byproduct of the execution across all aspects of our strategic framework for 2025. Gross profit was \$69.6 million in the quarter compared to \$70.3 million in the same period last year. Gross margin for the quarter was 41.7%, an increase of 26 basis points versus 41.5% in the prior year. This increase was primarily due to significant clearance activity in the prior year and not repeated in 2025.

SG&A, including R&D expenses for the second quarter was \$38 million versus \$38.9 million in the same period for the prior year. Overall, salaries increased for the company in the second quarter of 2025 compared to the second quarter of 2024. The increase is due to the furlough that occurred in 2024 that was offset by a decrease of transformational consulting fees.

Net income for the second quarter was \$10.9 million versus net income of \$17.1 million in the second quarter of 2024. Adjusted net income in the second quarter was \$10.6 million versus

adjusted net income of \$12.6 million in the same period of last year. Adjusted EBITDA for the quarter was \$36.4 million compared to \$38.3 million in the prior year, primarily due to higher growth among distribution partners, coupled with increased rebates and the absence of the furlough impact seen in 2024. Adjusted EBITDA margin was 21.9% versus 22.6% in the second quarter of 2024.

On Slide 15, you can see this quarter, we delivered record quarterly free cash flow of \$35.7 million compared to \$24.4 million in free cash flow for the same quarter a year ago. This performance was driven by continued improvements in operational efficiency and successful optimization of working capital across the business. While we're proud of the strong free cash flow performance this quarter, we're also very mindful of the headwinds ahead, particularly the potential impact of recently implemented tariffs.

With that in mind, let's turn to Page 16, where we've outlined the expected minimal net impact of tariffs on our free cash flow. As Matt had mentioned earlier, our team has been relentlessly focused on mitigating the impact of tariffs through a comprehensive set of strategies. And as you can see on 16, we have actions in motion that are expected to offset more than \$15 million in additional tariff-related costs between 2025 and 2026.

Despite ongoing inflationary pressures and the continually evolving tariff landscape, we remain proactive and disciplined in managing our operations. We project that the combination of our tariff mitigation initiatives and strategic pricing actions position us to fully offset tariff-related headwinds in 2025. Looking further ahead into 2026, we expect net pricing gains and mitigation efforts to not only absorb anticipated tariff costs but also support our ability to maintain strong free cash flow generation even in an environment of potentially lower volume.

On Slide 17, we reduced our covenant net leverage at the end of the second quarter to 4.22x versus 4.32x a quarter ago, which remains well under the 5x covenant when the revolver is drawn. At the end of the quarter, there was no outstanding balance on our revolver, and we continued -- concluded the quarter with \$63.8 million in cash and no expectation of drawing on the revolver in the near-term. This brings our total net debt to just under \$500 million for the quarter.

As a team, we are pleased with our execution in the first half of the year. We've built on the success of Q1 with core business growth again in the second quarter. As we move into the second half of the year, we are keeping a close eye on a mixed economic landscape. However, we have more clarity on expected tariffs for 2025, though broader trade conditions remain fluid. Therefore, with sales trending flat to start Q3 and mixed macro signals, we're taking a measured approach to our guidance. Our updated full year 2025 guidance reflects both the known effects of tariffs and consumer trends.

We are tightening our 2025 revenue range to \$580 million to \$595 million, which implies approximately a 2.2% growth at the midpoint over the core business base of roughly \$575

million in 2024. Additionally, we have tightened our range for our 2025 adjusted EBITDA guidance to \$116 million to \$127 million from \$113 million to \$130 million. Our first half results were stronger than originally expected and a direct result of the team's execution upon our strategic framework. While we continue to operate in an uncertain macro environment, we delivered two consecutive quarters of core business growth. We continue to build on this momentum and have better visibility on the impacts of known tariffs today, which are captured in our 2025 guidance.

While we remain mindful of the evolving environment and the fluid tariff situation, we are confident that the operational discipline and momentum we have built will continue to serve us well as we move through the balance of the year.

This concludes our prepared remarks. We would now like to open the line up for questions.

Operator

Thank you. We will now be conducting a question and answer session. If you would like to ask a question, please press Star 1 on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press Star 2 to remove yourself from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star key.

Your first question comes from Brian McNamara with Canaccord Genuity.

Brian McNamara

Congrats on the strong progress. First on pricing, how have your partners and enthusiasts overall responded to the price increases you put in and kind of the change in tact in terms of approaching your resellers with the 60-day notice? And with that, how would you characterize current sentiment in the marketplace? Has it improved with a little more certainty on tariffs? Any other color there would be helpful.

Matthew Stevenson

Sure. Brian, thanks for the question. When we look at just kind of that sentiment in June and just the overall out-the-door sales, they were strong in the marketplace. Now we notified to our distributors in April that price increase would take effect roughly in middle of June. And then July is historically one of the softest months of the year. But generally speaking, the feedback was -- the pricing was in line or lower than competitors in the relative categories. Of course, just given how many categories were present, that wide range of competitive dynamics exist. But overall, our pricing was definitely in line with the competition. And we just got to see in terms of just that overall elasticity of industry demand, pricing and discretionary spending, how that plays out once we get past the slower summer months and into more of the higher months of the year.

Operator

Next question, Christian Carlino with JPMorgan.

Christian Carlino

Follow-up on the prior question. Similar to how you're moving some sourcing to vendors in lower-cost countries, what are your conversations like with the resellers? Like are you winning share or shelf space because you're taking less price than the industry in addition to the channel expansion and product innovation work you've been doing?

Jesse Weaver

Christian, it's Jesse. It's a good question. I think all the indicators that we've got as we work much more closely with our distribution partners is that we are continuing to take share in the market. When we look at sort of our out-the-door growth relative to what the overall business is doing in these distribution partners, we continue to outperform there, and that continued all the way up through our most recent data, which is June. So, I think to Matt's earlier point, the pricing we put in was in line, if not better. and that is certainly helping us kind of continue to remain and gain momentum here.

Christian Carlino

Got it. That's helpful. And just given the full impact of the tariff cost increases should start to flow through in the second half, how are you thinking about gross margin for the year and maybe cadence over the back half? Understanding it's hard to predict consumer behavior and elasticities right now, but are you anticipating maybe higher prices overall, but key seasonal periods being more intense promotionally to maybe offset the impact to consumers' wallet? And just how you're thinking about that?

Jesse Weaver

We're not planning to do anything incremental from a promotional period. I mean, we've got a pretty strong partnership with our distribution partners on marketing calendar support in the back half. So, no intended changes there. We do anticipate, to your question on gross margins, to continue to maintain, if not increase gross margins in the back half, just relative to the pricing that we had taken, obviously. But I think our guidance in the back half kind of captures the squeeze on what you would expect in terms of margins there.

Operator

Next question, Joseph Altobello with Raymond James.

Martin

This is Martin on for Joe. My first question here is regarding sort of inventory. You've reduced so far by \$9 million. So, I was wondering if we can get an update on sell-through/sell-in?

Jesse Weaver

Yes. This is Jesse. I think we don't report out on the exact numbers we get from our distribution partners, but we're seeing really good numbers and results from them on the sell-out, and

that's kind of what we look at to understand just generally what the end user demand is. And I think that, that's a testament to our relative pricing, our continued enhancement in our partnerships with them and just making sure that we're partnering with them to make sure their inventory levels are in a good spot. So, I feel like the end distribution partner indicators are continuing to be really strong for us, particularly relative to what the rest of their business is doing.

Martin

Great. And I just want to touch really quickly on this free cash flow net impact bridge, very helpful, by the way. But you mentioned 2025 net pricing/volume it's going to be about a \$3 million tailwind. Earlier in the preamble, you had mentioned that about \$10.8 million in revenue was contributed from product innovation and strategic pricing. I also believe the PR said that product innovation was about \$8 million, which implies that strategic pricing was about \$2.8 million. Given that that's pretty close to that \$3 million number, does that sort of imply that there's going to be lower volumes in the back half of the year? Or what should be the read-through through that?

Jesse Weaver

So, I think those are two different metrics to be clear. The strategic pricing was an action that was taken earlier in the year to realign our channel margins with our distribution partners on some key product lines. So, those aren't necessarily related. As it relates to your question on the back half, I think generally, we feel like our visibility is much better than it was three months ago in the back half of the year. And we're just -- from a volume's perspective, as you can imply in the guidance, just taking a pretty conservative view relative to the back half, just given everything we're seeing in the economic indicators just generally around the consumer. But what we are seeing now, we feel like demand is holding up and the back half from what we can tell, is headed in the right direction to hit this guidance.

Operator

Next question, Phillip Blee with William Blair.

Phillip Blee

The product innovation growth is an interesting metric here. So, just curious around the level of new products that you've launched year-to-date and then maybe how that would compare to plans for next year or just steady state going forward, assuming we're past a lot of the tariff-related trade disruptions?

Matthew Stevenson

Yes. Phillip, this is Matt. Thanks for the question. Phillip, we're really focused on quality versus quantity. I mean we, of course, want to continue to drive the right innovations and, of course, increase the volume of those. When you think back to our strategic product rationalization that occurred where we took out basically about 45% of the portfolio, there was a lot of work being done for innovations that really weren't moving the needle. So, now we put in a very robust

phase gate system with seven gates to make sure we're bringing those right innovation to markets that are really going to drive the top line forward and to underline this organic growth trajectory. So, again, it's not about quantity, but for us, we want to continue to drive more revenue through innovation.

Phillip Blee

Okay. Makes sense. Great. And then now that you have some comfort around tariff mitigation, core business seems to be moving in the right direction. How are you thinking about free cash flow and capital allocation in the second half of the year and then maybe going forward? And then just timeline around reaching leverage around 3x?

Jesse Weaver

Great question, Phillip. And we obviously don't guide on free cash flow. I think as we've talked about historically, just given this guide, you can back into a free cash flow profile that would be about \$40 million to \$50 million at the current interest rates. I think we're on track to be in that range with better free cash flow in the back half this year versus last year. And just as a reminder, this time last year in Q3, Q4, we had some headwinds to the tune of \$6 million to \$8 million in each quarter from AP process changes.

So, we should continue to see positive free cash flow in the back half. And just in terms of capital allocation, we continue to maintain a pretty robust pipeline on M&A, but we are very conscientious on any transactions we look at as to sort of the net leverage profile on the back end. But in the absence of having a really good target in mind, we're going to continue to look at prepayment of debt like we've done historically. And this year, obviously, with that cash flow we've talked about, around \$23.8 million of it is used for the perpetual license on Cataclean which we look back and say it has really been a really good deal and growth driver for us.

Operator

Next question, Bret Jordan with Jefferies.

Patrick Buckley

This is Patrick Buckley on for Bret. On the new market growth, could you talk a bit about the trajectory of growth moving forward in Mexico and potential size there? And maybe how that strategy differs from the growth strategy in the U.S.? And I guess a quick follow-up there would be, is this the primary market expansion for the foreseeable future? Or are you guys seeing any other markets that you've identified for potential growth?

Matthew Stevenson

Yes, Patrick, thanks for the question. This is Matt. I mean, Mexico is just a natural market, of course, for us, just the adjacency to the -- and proximity to the U.S. and the amount of enthusiasts that are down there. And that was something that just was just not focused in years past. And how we look at the potential of Mexico, we would see that long term to be about 5% of the U.S. market is where we would see that. And it's going to take some time to get there,

right? It's really an all-do market entrance for us. It's everything from setting up distributors, setting up the proper product distribution, working with the national retailer footprint there. So, it's all going to take some time. But in terms of other markets, this is just a great market that we're spending the majority of our time on right now, again, for those reasons. But we -- there's a lot of enthusiasts around the globe, and we can continue to evaluate where it makes sense to plant a flag, so to speak, in a larger presence.

Patrick Buckley

Very helpful. That's all for us. Thanks.

Operator

Next question, Mike Baker with D.A. Davidson.

Mike Baker

Thanks, guys. Can I ask you, Jesse, you said flat sales so far in the third quarter. What's the base? In other words, is that including or excluding some of the one-timers from a year ago?

Jesse Weaver

Michael, we didn't -- we're trying not to speak specifically to the third quarter thus far, but I think what you implied from the script is kind of in line. And those trends we are seeing versus prior year as well as for the back half are embedded in our guidance. And your question around how does that compare to last year? I mean, I think to Matt's earlier comments, I mean, this is seasonally one of our lowest volume periods and demand is holding up relative to the prior year. And that's just on a gross basis. I think as we get into the back half, you're not -- there's only about \$3 million in each quarter related to divested businesses, and we're largely past the meaningful SKU rationalization that happened in the first half.

Mike Baker

Okay. Okay. And then I also wanted to ask just a little bit more detail on unit versus price in terms of your -- if we use a 3.9% sales growth in the second quarter, is there a way to break out how much of that was price versus unit?

Jesse Weaver

Yes. I think we put in the Q that actually volumes were pretty strong in the second quarter with a portion of it coming from price and unit growth. I mean year-to-date, unit growth has been positive with some pricing, obviously, to kind of get you over the 3% on the core business. So, we've been really pleased with how units have really picked up this year year-to-date. But as we mentioned, we're taking a bit of a conservative approach given what we're seeing in the economic indicators and just the magnitude of the pricing across the market and in the economy on units for the back half. But there's certainly some room for that to go north of what we're putting in our guidance.

Mike Baker

So, in other words, you've raised prices, you're not necessarily seeing unit degradation, but you are assuming that to be conservative in the back half?

Jesse Weaver

We're taking a conservative approach to it. But again, this is a business that you don't get a lot of visibility. But from what we can tell in our testing and trend evaluation and discussions with distribution partners, we feel like this is a good guide.

Operator

Next question, Joe Feldman with Telsey Advisory Group.

Joe Feldman

Thanks, guys, for taking my questions. I wanted to ask about just your view of the consumer at this point. I know you said summer is always a soft period and you pass through price increases now, so it's a little hard to tell. But I mean, what the customer has been buying, at least in the second quarter, are you seeing people stepping up? Are they adjusting their spend? It sounds like unit sales are up. So, I assume that's a good thing. People are kind of back at the projects. But just how do you view the consumer right now?

Matthew Stevenson

Joe, it's Matt. Thanks for the question. As I commented, Joe, the out-the-door sellout in June was really good. And so, generally speaking, to Jesse's point, what we saw on units for the first half of the year, there's a couple of components. I mean, overall, the market is hanging in there, but more importantly, we're taking share, right? And so, now that you have that price increase that goes through in June, July typically is that softer or one of the softest months just due to a lot of back-to-school summer vacations and things that go on. So right now, we haven't seen anything meaningful one way or the other, but it will -- we'll get more color here as the third quarter plays out. But right now, nothing meaningful one way or the other from what we've been seeing.

Joe Feldman

Got it. And then maybe just a follow-up for Jesse. With regard to the guidance, I know you're not giving too many specifics, but like are there any puts and takes we should think about in the second half? Like is there anything unique about maybe third quarter versus fourth quarter this year? Or should we -- are we safe to use kind of the last year kind of flow to get us to the numbers for the full year?

Jesse Weaver

Yes. I would say just as a reminder, in the back half, usually Q3 is slightly lower than Q4, just with our end of year Holley Days is a really big sales cycle for us. When you think about -- we're not going to give necessarily the quarterly guidance on the top line, but it's usually around like a 48% in the third quarter -- 49% in the third quarter with slightly more, obviously, in the fourth.

And then we've talked about sort of our operational initiatives and the pricing, and a lot of that stuff is kind of helping bolster margin on a year-over-year basis as we go into the back half.

Operator

Next question, Brian McNamara with Canaccord Genuity.

Brian McNamara

Thanks for the follow-up here. So, great job on the tariff mitigation. Looking at Slide 11, it looks like \$8.5 million out of the \$15 million in tariff mitigation is relocation with existing suppliers and sourcing with new suppliers in lower-cost countries. I was wondering if we could get a little color there, specifically on how your exposure to China, maybe some of the higher-cost countries is changing and then what kind of lower-cost countries you're kind of shifting to? China sourcing exposure is a consistent question we get from investors.

Matthew Stevenson

Yes, Brian, I'd say our overall strategy had a number of facets to it, as you could see in the prepared material. But overall, we want to be in countries that have a more stable long-term relationship with the United States, and that's where we've been focusing on either relocating with our current suppliers or finding new suppliers in lower-cost countries. So, that's just been the main focus and mitigating that exposure in China.

Brian McNamara

And then at risk of beating a dead horse on the H2 guide, and maybe I'll try it a different way. So, it calls for a big deceleration in organic sales. I think it's up less than 1% despite you're lapping much easier comps. And I know July is typically a slow month, so -- and you mentioned it's flat. I guess why wouldn't all the heavy lifting you've done internally kind of help achieve a little bit better H2 growth? Or is it just simply conservatism on your part?

Jesse Weaver

Yes. I think, Brian, again, we all have been saying the back half is the biggest question mark just given what we were all seeing in April with the consumer and the tariffs and the pricing flowing through. And so, we were really just taking like to your point, a bit of a conservative view on what the units are going to do. I mean, I think we've all read the headlines of the pricing across the economy starting to actually flow through and what's going on with just employment. And we're in the thick of all of that right now. And if you give us a couple more months, obviously, we'll be in a much better position. And we're just not in the position where we feel like it's prudent to lean out until we know more.

Brian McNamara

Fair enough. Thanks, guys. Appreciate it.

Operator

I would like to turn the floor over to Matthew Stevenson for closing remarks.

Matthew Stevenson

All right. Thank you, Stacy. Slide 20 underscores the compelling investment thesis behind Holley Performance Brands. At the heart of this story is a passionate and deeply engaged automotive enthusiast community. For our customers, this is far more than a past time. It's a lifestyle rooted in performance, personalization and pride. With an addressable market exceeding \$40 billion, Holley is uniquely positioned as the industry leader, powered by a portfolio of iconic brands recognized for decades of innovation and excellence. Our growth story is grounded in a proven track record of successful acquisitions and disciplined integration. We consistently created value by expanding our reach, enhancing capabilities and unlocking synergies across the platform.

Looking ahead, we see a transformative opportunity to redefine how both consumers and distribution partners interact with our brands. Through expanded digital capabilities and omnichannel engagement, we're building a new frontier that strengthens loyalty, accelerates conversion and expands access.

Now as we emerge from our multiyear transformation and return to growth in our core business, our financial ambitions are clear. We remain focused on delivering sustainable organic growth, maintaining gross margins of 40% and achieving adjusted EBITDA margins greater than 20%. At the same time, we are committed to generating strong, consistent free cash flow and to building a disciplined M&A platform that unlocks long-term value. Together, our powerful enthusiast ecosystem and Holley's trusted best-in-class brand portfolio represent a rare and differentiated investment opportunity.

In closing, I want to thank our dedicated team members for their tireless efforts to commitment to excellence, our loyal consumers who bring our brands to life and our valued distribution partners, many of whom have been with us for decades. Your partnership and passion continue to drive Holley forward. I want to thank you for your attendance on our call today and wish you all a great morning. Thank you.

Operator

This concludes today's teleconference. You may disconnect your lines at this time and thank you for your participation.