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GGG.N - Q4 2024 Graco Inc Earnings Call

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OVERVIEW:

Company Summary

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Mike Halloran *Robert W. Baird & Co - Analyst*

Saree Boroditsky *Jefferies Group LLC - Analyst*

Matt Summerville *D.A. Davidson & Co - Analyst*

Bryan Blair *Oppenheimer & Co. Inc - Analyst*

Joe Ritchie *Goldman Sachs Group Inc - Analyst*

Jeff Hammond *KeyBanc Capital Markets Inc - Analyst*

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PRESENTATION

Operator

Good morning and welcome to the fourth-quarter conference call for Graco Inc.

If you wish to access the replay for this call, you may do so by visiting the company website at www.graco.com.

Graco has additional information available in a PowerPoint slide presentation which is available as part of the webcast player. At the request of the company, we will open the conference up for your questions and answers after the opening remarks from management. During this call, various remarks may be made by management about their expectations, plans and prospects for the future. These remarks constitute forward-looking statements for the purposes of the Safe Harbor provisions of the Private Securities Litigation Reform Act. Actual results may differ materially from those indicated as a result of various risk factors including those identified in Item 1A of the company's 2023 annual report on Form 10-K and in Item 1A of the company's most recent quarterly report on Form 10-Q. These reports are available on the company's website at www.graco.com and the SEC's website at www.sec.gov. Forward-looking statements reflect management's current views and speak only as of the time they are made. The company undertakes no obligation to update these statements in light of new information or future events.

I will now turn the conference over to Chris Knutson, Vice President, Controller and Chief Accounting Officer.

Christopher Knutson - *Graco Inc - Executive Vice President, Corporate Controller*

Good morning, everyone and thank you for joining our call.

I'm here today with Mark Sheahan and David Lowe.

I will provide a brief overview of our quarterly results before turning the call over to Mark for additional commentary.

Yesterday, Graco reported fourth quarter sales of $549 million, a decrease of 3% from the same quarter last year. Acquisitions contributed 3% sales growth in the quarter. Excluding acquisitions, fourth quarter sales decreased 6%. The effect of currency translation had no significant impact on sales. Reported net earnings decreased 1% to $109 million for the quarter or $0.63 per diluted share. Excluding the impact of business reorganization charges, excess tax benefits from stock option exercises and other prior year items, adjusted non-GAAP net earnings were $110 million or $0.64 per diluted share, a decrease of 20%. The gross margin rate decreased 200 basis points in the quarter. Realized pricing was not enough to offset sales volume declines occurring in all segments, unfavorable product and channel mix and acquisition related impacts. Machining and assembly hours declined on lower sales volume and inventory reduction efforts.

Total operating expenses increased $19 million or 15% in the quarter mainly due to business reorganization costs of $7 million, expenses from acquired operations of $7 million and litigation costs in the contractor segment associated with a trial that concluded in December of 2024 of $7 million. Total spend related to this legal matter was $9 million for the quarter and $16 million for the year. Reductions in volume and earnings-based expenses of $6 million partially offset this increase. Lower gross margin along with increased expenses during the quarter resulted in an operating margin rate of 24% compared to 30% for the same quarter last year. Excluding business reorganization costs, industrial segment operating margin rate for the quarter was 33% compared to 37% for the same quarter last year.

And the process segment operating margin rate for the quarter was 29% compared to 28% for the same quarter last year. Excluding acquisitions and related costs, business reorganization charges and litigation spending previously mentioned, contractor segment operating margin rate for the quarter was 27% compared to 29% for the same quarter last year. Total company operating margin rate excluding these impacts for the quarter was 29%, a decline of 1 percentage point compared to the same quarter last year. Excluding the impact of the pension settlement charge in 2023, interest and other increased $2 million during the quarter driven primarily by increased interest income on cash held. The adjusted effective tax rate was 21.5% for the quarter due mainly to the unfavorable effects of foreign earnings taxed at higher rates.

Cash provided by operations totaled $622 million for the year, a decrease of $29 million from last year driven mostly by lower net earnings. Cash provided by operations as a percent of reported net earnings is 128% for the year. Significant year-to-date uses of cash include repurchases of 399,000 shares for $31 million, acquisitions of $242 million, dividends of $172 million and capital expenditures of $107 million of which, $67 million related to facility expansion projects. These cash uses were offset by share issuances of $66 million.

A few comments as we move forward to 2025. Based on current exchange rates, assuming the same volumes, mix of products and mix of business by currency as in 2024, movement in foreign currencies would have an unfavorable impact of approximately 1 percentage point on net sales and 2 percentage points on net earnings for the full year of 2025. Unallocated corporate expenses are projected to be $39 million to $42 million. The effective tax rate is expected to be 19.5% to 20.5%, excluding any impact from excess tax benefits from stock -- related to stock option exercises and other one-time items. We expect capital expenditures to be approximately $50 million to $60 million as we have now completed expansion projects for nearly all of our operations.

And finally, effective January 1, 2025, the company moved to a global customer centric operating structure resulting in a non-recurring business reorganization charge of $8 million in the fourth quarter. Annual savings is estimated to be approximately $16 million. The new operating structure consists of three segments: industrial, expansion markets and contractor. The industrial segment consists of the newly formed industrial division and the powder division. The company's previous industrial and lubrication equipment divisions along with the process transfer equipment business that was part of the company's process division combined to form the new global industrial division. The powder division remains unchanged. The company's environmental, semiconductor, high pressure valves and electric motors businesses together with select future ventures and acquisitions in new or adjacent markets have been combined to create the newly formed expansion market segment.

The contractor segment remains unchanged as a reporting segment relative to prior periods. Segment operating results will be reported under the new organizational structure beginning with the first quarter of 2025. Segment information recast to conform to this new structure is available as supplemental information.

I'll now turn the call over to Mark for further segment and regional commentary.

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Thank you, Chris. Good morning, everyone.

All my comments will be on an organic constant currency basis.

I'd like to start today by welcoming Corob to the Graco team. We closed the acquisition in November and integration activities are underway. Initial results have been as expected, generating 3% revenue growth in the fourth quarter. Corob brings high tech dispensing and mixing solutions to Graco in the growing paint and coating machinery and manufacturing category. This acquisition will enable us to leverage our existing products and channel while expanding our global manufacturing footprint. Overall, the year has been challenging and the business landscape has been soft across many of our end markets. Declines in key industrial markets in China along with weakness in our semiconductor business drove much of the decline during the year.

The softness continued into the fourth quarter resulting in a 6% sales decline. These results were driven by lower sales volume in all segments and regions except process, North America and contractor, Asia Pacific. Sales in the process segment improved during the quarter as we had growth across major project categories including vehicle service, industrial lubrication and environmental. While we continue to see revenue declines in the semiconductor markets globally, we had growth in North America in the quarter and have seen positive booking momentum in all regions.

Protective coatings activities remain strong with growth in all regions. In particular, the container market has improved throughout the year in Asia Pacific. As Chris previously discussed, the reported results were lower during the fourth quarter compared to the rest of the year. However, excluding initiatives and unusual items in the quarter, revenue declined 6% resulting in a 12% reduction in operating earnings, which is consistent with the full year. The slower markets allowed us to speed up our M&A and reorganization activities that we believe will set us up for future growth. As we enter 2025, we expect these initiatives to drive incremental volume along with our pricing actions resulting in strong incremental margins.

In addition, our M&A pipeline remains active, and we're excited about the possibilities the new organizational structure can bring as we focus on new and adjacent markets.

Now turning to some commentary on our segments and regions. Contractor declined 3% for the quarter and was down 1% for the year driven primarily by softness in the US housing and remodeling markets. Protective coatings were a bright spot with growth across all regions for both the fourth quarter and for the year. Steady performance in this market has been helped by infrastructure investments, increases in container market along with rail, marine and fireproofing. While the current construction environment remains mixed and pressures on housing affordability are likely to continue, our new products have been successful and are expected to contribute to growth.

During the fourth quarter, we launched the new PowerShot XT electronic powered airless paint gun which allows contractors to spray all day on a single charge. This product along with additional 2025 releases and the full year impact of our 2024 launches gives us optimism as we enter the new year despite a mixed picture in the global construction markets. Industrial segment revenue declined 13% for the quarter and was down 6% for the full year. China was weak particularly in our sealants and adhesives products which impacts many of our key end markets such as automotive, solar and battery.

Despite the revenue declines, incoming order activity in China throughout 2024 has been steady albeit at a lower level than 2023. We have seen positive signs as coating activity has been improving and our sales team has expressed optimism as we enter the new year. The timing of completion and acceptance of powder finishing systems also resulted in a decline in the quarter. Booking activity in the powder division has improved and we carry a slightly larger than normal backlog into the new year. Despite the tough year, the new industrial teams are energized by the full suite of Graco products and are focused on executing under the new customer centric approach.

Process was flat for the quarter but down 8% for the year. Growth across Americas was offset by declines across EMEA and Asia Pacific. Sales in the fourth quarter were the largest of the year and grew sequentially by 13%. Total revenue for the quarter was consistent with the prior year quarterly run rates. Order activity increased low double digits for the quarter and our quarterly bookings were the largest we have seen in the past two years. However, backlog is back to normal which contributed heavily to the prior year sales, especially in the semiconductor market.

Moving on to our outlook. Our team demonstrated resilience, overcoming both commercial and operational obstacles in a challenging year with the dedication and resolve to define our company. We continue to generate strong cash flow, and our balance sheet gives us flexibility. Over the past five years, we've invested heavily in our manufacturing footprint and automation capabilities which puts us in a good position to meet future demand. Heading into 2025, we do anticipate that some of the challenging end market conditions we experienced last year will persist, but we are optimistic that the worst is behind us. Therefore, we are initiating a full year outlook for 2025 of low single digit sales growth on an organic constant currency basis.

In closing, I'd like to thank our employees, suppliers, customers and distributor partners around the world for their contributions throughout the year. It's been challenging but in Graco fashion, we've been able to overcome the hurdles and set ourselves up for future long term growth.

While there are many things that contribute to our culture, it's our loyal and hard working employees that make this company great.

That concludes our prepared remarks.

Operator, we're ready for the first question.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Deane Dray, RBC Capital Markets.

Deane Dray - *RBC Capital Markets - Analyst*

Mark, you provided good color regarding geographies and end markets. But can you just frame for us how about versus your expectations? I mean China has been weak, but it sounded like it stayed weak and same on semiconductor being soft. But just kind of versus your expectations about the quarter. And then you also typically provide orders for the past six weeks. You said things have been steady. But if you could give us that data point, that would be a great start.

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. I'll give it a shot here. I think expectation-wise, I would say that our process division overperformed our expectations and I think it was mostly in areas our environmental business was good, our LED businesses were good. And our high-pressure valve business was also good. And I would say that came in a little bit stronger than what we had hoped in the booking activity there looks pretty good too as we head into 2025. I would say industrial came in less than what we were expecting. They did have a very tough comp in the fourth quarter. We knew that. We were expecting that their revenues could be impacted by that. But really the declines in Asia Pacific and in our sealant and adhesive business were pretty sharp compared to what we experienced last year in Q4.

And then contractor I think also underperformed a little bit in terms of our expectations. We just didn't see the large kind of year end orders that we might have normally gotten in a normal year. And I think that had something to do with the fact that the conditions are still fairly sluggish across a lot of the end markets. And we experienced that really throughout the year. So if I look at the full year contractor business being down 1%, I think is really good performance in a challenging economic environment.

When it comes to the order rates and outlook and how we got to the low single digit guide, I mean we really did look at what we've seen in the back half of last year to help guide us in putting those numbers together and then comparing that to what we actually experienced on the billing side and that's how we got to those numbers. And I would say that with regard to the recent activity that we've seen, I think it kind of lines up with the guide at this point.

Deane Dray - *RBC Capital Markets - Analyst*

And just the second question, I know we're still early in the process, but lots of questions and anticipations of how tariffs might play out. And Graco is in a unique position and look, this is not new. We've been through this before, but just a lot of this is reminding us. But the idea here, you're unique in that. You have a concentrated manufacturing footprint in the Minneapolis area less globally than some of your peers. How does that present itself, as a risk or just different impact on tariffs? And how does that factor into your typical January price increase, one price increase per year? Would you delay that? How might that impact as well?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

We didn't specifically factor tariffs in because a lot of times, well, when you put your price list out and you talk to distributors, you got to give them enough notice ahead of time. So we did that kind of late third quarter, early fourth quarter of '24 before all the tariff talk became more significant. We have run some math here at the company. We don't claim to be experts when it comes to what's actually going to get implemented versus what's talked about. But at least in terms of what we've heard of verbalized and what impact it might have to Graco, it looks like it's something that we could manage.

We didn't factor it into the January price increase, but as you know, if we need to, we could always make a decision to do some other pricing actions if it becomes more significant for us. What I will say is that the talk that we've heard with respect to tax rates is interesting. The discussion about providing preferential corporate tax rates for companies that manufacture in the United States, that could be really nice for us because we, as you know, have a footprint that is really highly concentrated here in North America. And so to the extent that does take shape, that could be beneficial to Graco.

Operator

(Operator Instructions) Mike Halloran, Baird.

Mike Halloran - *Robert W. Baird & Co - Analyst*

So just clarifying the outlook quick. If I peel that back, it sounds like you're saying if you look at the current order rates and then you layer on, call it normal conversion based on last year's incidences and call it relatively normal seasonality, that's how you get to the low single digits? In other words, not really embedding any real improvement here. Just kind of a steady state from current levels and that should be enough or am I missing that?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. I think that's accurate. I mean I always tell people -- I think I've told you personally that our ability to forecast isn't real great just because of the fact that we're such a short cycle business. But as I think we said in the comments, the incoming levels of orders have been fairly consistent throughout the back half of the year. And so we feel confident. At least it feels like things have evened out. We do have our pricing actions which should be helpful. We've got some new products that we're launching, which should be helpful. And all of that factored into our analysis and what we're coming up with on the outlook for the year.

David Lowe - *Graco Inc - Chief Financial Officer, Treasurer*

Yeah. This is David. I would add that again, going back to the comments, the -- I would say the big negatives, the areas that we've talked about in China, in particular, in our industrial, specifically our adhesive and sealant space as well as the semiconductor space, with the rates that we see now, the big negatives that we were experiencing throughout the year have flatlined. And with the sort of performance we saw in most of our businesses in 2024 and certainly in the back half along with what I would say flattish performance in those three or four markets that had been excessively negative give us a pretty good degree of comfort that we should be looking at growth with normal seasonality in markets like contractor.

Mike Halloran - *Robert W. Baird & Co - Analyst*

And then two margin questions if I may. First, Chris was a speed beam in there which I appreciate. However, just want to make sure I understand the moving pieces on the contractor margins. So I think you were implying 27% of the apples for apples to margins versus last year I think excluding all the one timers and excluding the acquisition. If you think about what the margin would look like on a forward base or just in this quarter, if you exclude, called the step up charges associated with bringing Corob, what would that look like and how do we think about what the representative run rate looks like from here once all that's normalized?

Christopher Knutson - *Graco Inc - Executive Vice President, Corporate Controller*

So I think, Mike, with the step up charges, we've had one time charges related to the acquisition of about $3 million in there. So if you take that into account with the contractor, you're probably going to look at somewhere for this quarter, somewhere in that 25% to 26% range if you just subtract everything else out.

Mike Halloran - *Robert W. Baird & Co - Analyst*

And then the reorganization savings. It's a big number, a little bigger than what I was expecting. Twofold, one, is that expected to be realized starting in the first quarter? And then secondarily, how does that shake out across the segments and where does that show up?

David Lowe - *Graco Inc - Chief Financial Officer, Treasurer*

I would say, yes, it should start right away. The -- there was a concerted effort to get the hard -- I'd say that the heavy lifting done in Q4, and it was completed. And that's reflect -- the cost side of it is reflected in the charges. And across the organization, we're working with the new arrangement. And so you should see those benefits beginning right in the beginning of the -- here in the first quarter.

I would say that in terms of thinking about the segments under the new structure, the heaviest lifting was certainly done in the contractor space where we were -- in the industrial space, where we were combining several different parts of the legacy Graco organization. But contractor and the expansion markets also played a role and you'll see benefits in varying degrees across all three.

Christopher Knutson - *Graco Inc - Executive Vice President, Corporate Controller*

I will say, Mike, if you're going to split it out between the different segments, that the charges as they're put in there for each of the segments today is a good proxy as to what the savings will run next year. And as you put it into the new segment structure, we're moving about two-thirds of the revenue from the process segment to industrial and the cost and the savings should be allocated similarly.

Operator

Saree Boroditsky, Jefferies.

Saree Boroditsky - *Jefferies Group LLC - Analyst*

So just building on the orders questions, I think during the last earnings call, you saw some improvement in the incoming order rates over the prior six weeks. In this release, you guys have obviously talked about consistent rates in the fourth quarter. So did you see orders slow down post October and what have you seen more recently?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. We did see a little bit of a slowdown. It kind of surprised us. I want to say the November, December orders were softer than what we had seen in the early part of the quarter. And in terms of how it -- how the quarter played out versus my expectations, I think I answered that previously. Pretty good and the process grew a little bit of a disappointment and contractor and a larger disappointment in the industrial. And the recent -- the most recent order trends that we've seen, again, we believe that they're supportive of the low single digit guide that we've given for the year.

Saree Boroditsky - *Jefferies Group LLC - Analyst*

And then your 2025 outlook chart, I believe you used your prior segment. So just curious if you could break it out on how you're thinking about the updated industrial and expansion markets in your traditional pie chart framework.

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. Again, I do believe that we are looking for growth in both those groups on a full year basis, but we do recognize that there still will be some challenges and I think that that's really what we tried to reflect in the charts.

Operator

Matt Summerville, D.A. Davidson.

Matt Summerville - *D.A. Davidson & Co - Analyst*

So Mark, with respect to this reorganization and kind of Graco's historical M&A practice, how are you changing the way the net is cast if you will and what kinds of things are you may be willing to look at that maybe wouldn't have hit the radar screen of some of your predecessors? How should we be thinking about that?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. It's a good question and I might actually just expand a little bit to talk a little bit about why we're doing the reorg and what we expect to get from it. M&A is part of it, but it's not the full story.

So really there's a number of things that we believe are going to be the result of what we've done. Number one, we want to leverage our customers and our channel better by combining the industrial, the LED, the process group with the diaphragm pumps. We really do believe that we'll be able to offer a more full complete picture of Graco product to our channel partners as opposed to having several people interact with those channel partners and their customers.

The customers are very common across those product lines and the channel partners are also very common. So that is one thing that we hope to get. We also hope to have operational efficiencies by eliminating a lot of the overlap that existed in the company across those separate business

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units and primarily, in the areas of sales, marketing and engineering. And that's really what you've seen in terms of the benefits that we're going to get out of the costs that we've taken out.

We also will be focusing more on a global organization, taking down the matrix structure that we had previously. So that our teams can focus on global customers and global accounts and make the investment decisions and allocate the resources appropriately as they see fit and not have to go to a regional leader to ask for approval and to get the allocation of the funds and the resources that they need that way.

With respect to M&A, we created this group called Expansion Markets. And what we put in there were our legacy semiconductor business, our environmental business and our high-pressure valve business. And we've asked that team to really evaluate those assets and look for ways to expand them really with a focus on can we do more in those areas? Do we like them? We think that there's opportunities and if we put up a focus on it, we think that there's a better chance of us being able to expand there.

But in addition to that, we've also asked that group to work with our strategy team and our corporate development team to look for new sandboxes for Graco to plan beyond the stuff that we would have looked at historically. We are sorting through some areas right now. We got a couple of things that we're looking at. I don't want to share those with you, but we're talking about fairly sizable fluid handling markets and applications that the company hasn't historically been involved with. And we do the detailed work. We want to make sure that it makes sense. We want to figure out the strategic fit for the company and to the extent that things line up. Then we start to identify targets, and we go after those things.

So I think it opens up the lens a little bit for us. We never really had anybody at the company that was looking beyond what we currently had in the portfolio. And so I think that that's really what that group is charged with doing.

Matt Summerville - *D.A. Davidson & Co - Analyst*

As a follow up and maybe I just missed it, I don't remember you guys talking about this sort of litigation that was seemingly ongoing for a period that has since wrapped up. Can you maybe talk a little bit about the genesis and kind of the conclusion? And I guess did I hear that you've had $16 million of what we should consider to be non-recurring charges this year? And I guess would that have hit the segment? Would that have hit corporate? More detail on that would be helpful.

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. $16 million is a correct number. It was in the contractor business. It was litigation that I really don't want to comment about. It's done. It's been taken care of and we're going to move off of it.

Matt Summerville - *D.A. Davidson & Co - Analyst*

So all of it -- just to be clear, Mark, all of that $16 million hit contractor segment operating profit and you did -- in none of your financials, you did not non-GAAP any of that out this year, correct?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

That is correct. Yeah. We -- that was the full year number and I think we had what, $8 million or $9 million in the fourth quarter.

Christopher Knutson - *Graco Inc - Executive Vice President, Corporate Controller*

$9 million in the fourth quarter.

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

We did -- the segment chart on I think page 13 of the slide deck for contractor does a pretty good job of breaking the special items out including the litigation.

Operator

Bryan Blair, Oppenheimer.

Bryan Blair - *Oppenheimer & Co. Inc - Analyst*

I was hoping if you could offer a little more color on the early innings of Corob integration. What continues to excite your team? If there have been any surprises to date? And you having now owned the asset for a bit, curious if you're willing to share 2025 outlook for revenue and margin contribution. And perhaps more importantly, looking forward, where your team thinks profitability can climb medium term?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. I'd say it's early days, Bryan, but we've been pleased with the revenue so far. I mean for the eight weeks that we've owned it or whatever it's been. We like the team a lot. We feel pretty confident that they've got good momentum as we enter into 2025. We are expecting growth. It's not going to be anything heroic but probably the low single digit growth for that group is what we're aiming for 2025. And all in all, we're excited on a number of fronts, but in particular, the business, it doesn't have a tremendously strong footprint here in North America. And we believe that with the great brand that we have and the good reputation that Graco has with some of the larger companies that purchase this equipment, we feel like we'll at least have a good chance at being able to introduce Corob to those customers. Whether we're successful or not is really depends on us and how good of a job that we do. But we think that it could open up some doors that the Corob would have had a harder time opening on their own as a smaller independent company.

Bryan Blair - *Oppenheimer & Co. Inc - Analyst*

It's encouraging to hear that you're expecting growth in China for the year admittedly against easy comps. But nonetheless, that momentum is a good guide. I'm wondering if you could just offer a little more detail on what you're seeing on a run rate basis and perhaps comments on whether Corob relationships factor into or influence your confidence in returning to growth this year.

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. I think with respect to China, it's more of the Graco legacy business. We think we've kind of gotten through the worst of it. I would say that it's, I'll call it plateaued or gotten to the point where we've reached equilibrium, and our hope is that now that we'll get some upside as the market grows a little bit and we implement our pricing actions, and our team feels fairly confident. Obviously, we have easier comps that factors into the equation as well.

So it's more on the legacy side of the operation that we feel like China should get back to a growth trajectory here in 2025. Corob does give us a little bit more exposure in AP. We're excited about their India manufacturing footprint. We think that there's some opportunities there for us to perhaps leverage that. And it just gives us a little bit more of a presence in that country where I think as I said before, that's a country that we've had on our radar for a while to grow the Graco presence.

David Lowe - *Graco Inc - Chief Financial Officer, Treasurer*

I should leave well enough alone. I would just add, we did have some nice feedback from the new industrial sales team and leadership in China last week. And optimistic going into this year, even about some areas that were soft for us, very soft for us in 2024. Markets like battery, solar and automotive. And we see some -- we already are seeing a little bit of project activity that was absent during much of the year last year.

Operator

Joe Ritchie, Goldman Sachs.

Joe Ritchie - *Goldman Sachs Group Inc - Analyst*

So I'm just trying to make sure I fully understand the one-off that could be potential good guy in 2025. And so if I'm looking at slide 5, you've got the business reorg cost of $8 million that goes away, the incremental litigation costs of $13 million that goes away. And I think I heard you say that there's the savings from the reorg is a -- it should be $16 million. Is that all expected in 2025, and did I get all of that right?

Christopher Knutson - *Graco Inc - Executive Vice President, Corporate Controller*

I will say, Joe, on the litigation, that is the change from '23 to '24. The total spend for the year on the litigation was $16 million that'll go away. But you did get the other pieces right.

Joe Ritchie - *Goldman Sachs Group Inc - Analyst*

So about $40 million in total. Is there anything that should be offsetting this? Obviously, we'll get a better understanding of how volumes turn out for the year but any major offsets we need to consider from a margin standpoint?

Christopher Knutson - *Graco Inc - Executive Vice President, Corporate Controller*

So I don't see anything that would be major that would offset that.

Joe Ritchie - *Goldman Sachs Group Inc - Analyst*

And then my one last question, and just thinking about the expansion markets, clearly, it was very helpful to have all the supplemental data going back to '22. Clearly '22, '23, great growth years. '24, the expansion markets were down quite a bit. I guess as you kind of think about -- it's kind of odd to see expansion markets down but I know that there's probably some tough comps there as well. But as you think about the trajectory of those businesses in 2025, is the assumption that these businesses will outgrow your remaining portfolio and just any color around that would be helpful.

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. I think if you were to look at the pieces, I think the semiconductor is really the wild card there. And that was the main reason for the reduction in '24. And we do expect that that market is going to be firmer and that we'll get back to a little bit of growth there in that '25. The other two businesses have been pretty steady performers with some decent growth here in '24 for our environmental business. We kind of expect that to continue. And same thing on the high-pressure valve.

Operator

Jeff Hammond, KeyBanc Capital Markets.

Jeff Hammond - *KeyBanc Capital Markets Inc - Analyst*

Just on a contractor, a couple questions. One, last year, I think your new product timing was more 2Q versus 1Q based on time. And I'm just wondering how you're thinking about that comp and new products coming in. And then just with kind of rates stuck high, lower existing homes, lower new home sales, kind of what you're hearing from the field paint stores contractors about just the paint business in particular?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. You're right. I think you're correct that our new product launches last year came in a little bit late for CED. I think they were in Q2 versus Q1. So perhaps that creates a little bit easier comp for them in the first quarter than what you might see in the second quarter. But I'll let you guys figure that out and do the modeling on that piece of it. The market itself, I think is, I'll call it stable to potentially improving. Housing starts are kind of projected to be flat here in '25. New home sales are projected to come up a little bit. And that does help us because every time somebody moves, they tend to fix it up or paint it and then the new people move in, and they repaint it again. So to the extent that the existing home sales actually trend up, I think that would be favorable for us.

Remodelings kind of hanging in there. Interest rates, like you guys know more about that than I do, but they appear to be stable to maybe slightly favorable for us. And I think on the commercial side, we're expecting just a real small amount of growth there as well. So you put the whole thing together and I feel like it's at least as favorable market as what we've had in the last couple of years, maybe a little bit of upside.

Jeff Hammond - *KeyBanc Capital Markets Inc - Analyst*

And then just on the comment about timing and powder coatings. Is that business that shifted from 4Q to 1Q and is there a magnitude you can give?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

I don't think so. I think that really, it really relates back to, if you look at last year's Q4 and you look at the industrial numbers that was put up, a lot of that was like powder project activity. And so the fact that we just didn't get that in Q4 this year really created kind of a tough comp for that group. I think we said in the comments that their backlog right now is actually a little bit higher than what it would normally be. So we feel pretty good about how things are trending here for that part of the business as we head into '25. I don't think there's any real meaningful shift that you should be thinking about from this should have gone in '24 but it's going to wind up in '25.

David Lowe - *Graco Inc - Chief Financial Officer, Treasurer*

Yeah, that's the one -- that's certainly one area where we have a little longer visibility than in most of our legacy businesses. Mark's right. We're carrying what looks to be a little bit of a backlog above normalized levels for the size of the business. And we also saw some firmness in, I would say order rates as the fourth quarter wound up. That left us with a, I would say a positive ish feeling as we get into this year and bodes well maybe not just for Q1 and Q2, but how the business could play out on the second half of the year.

Jeff Hammond - *KeyBanc Capital Markets Inc - Analyst*

And then just last one on the one timer. So $3 million of step up from the acquisition. Is that done or do you have some carry over in the first half?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

We'll have some carry over through the first quarter. But after the first quarter, we'll have gone through all of the step up.

Operator

Ross Sparenblek, William Blair.

Sam Karlov - *William Blair & Company - Analyst*

This is Sam Karlov on for Ross.

Regarding the strength in the legacy America's process segment, is there anything to read into as it relates to QUANTM electric pumps? And are there any updates on where you think you are in the customer trial phase?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. I don't think there's anything in particular. I think it was just across the board kind of general strength. A lot of it actually was in our lubrication businesses which have been good, but they did have a nice strong finish of the year.

Operator

(Operator Instructions)

Andrew Buscaglia, BNP Paribas.

Andrew Buscaglia - *BNP Paribas - Analyst*

Yeah. I just wanted to clarify. So I mean a little extra commentary on Corob. Yeah. So it sounds like we should assume sort of mid-single digit contribution to sales this year. Could you clarify that? And then what about quantifying anything on EPS accretion? Whether it's year one or year two, can you make any statements there?

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. I think the mid-single digit -- low single. Well, I think if you just annualize the revenue, I mean it's probably 4% to 5%. It'll help our growth rate in 2025. So you just add that on top. And I think we're looking at it to be slightly accretive of the EPS for the full year, but Chris would -- he would give --

Christopher Knutson - *Graco Inc - Executive Vice President, Corporate Controller*

It's probably going to be accretive in 2026 for the full year as we get through some of the one-time costs and things happening this year. That's kind of the estimate right now.

Andrew Buscaglia - *BNP Paribas - Analyst*

And then, obviously, you guys are signaling a little bit more M&A ahead potentially. Can you talk about your thoughts on accretion when you make these deals? And then for investors that might be concerned around your return on invested capital, which is very strong, any thoughts about how you're thinking about returns and protecting that number?

David Lowe - *Graco Inc - Chief Financial Officer, Treasurer*

Well, we definitely think that buyer's discipline is the way that we justify any major capital project. And philosophically, that's the way we try to approach our acquisitions, which is one of the reasons why over the last couple of years, we -- there have been some interesting transactions and some large transactions, but the multiples have been pretty -- have remained, I'd say a little more elevated some of the deals in the niche industrial space, especially if they're in the pharma or the healthcare or some of the higher growth spaces.

And with all that said, that we are optimistic that the sell side activity, especially on the part of the PE companies could represent an opportunity for some interesting business opportunities. Our team in development stays very close to the banks and they have reasons to believe there could be some interesting meaningfully sized properties in the flow control space coming to market later in the -- in Q1 and Q2. So we're looking -- I would say we're looking for good merchandise. That's number one. That I've learned from experience is we want to buy good businesses. And yes, you do have to maintain a buyer's discipline. And we will see with changes in interest rates and with decent properties coming to market how that plays out in the upcoming year, but we remain very optimistic. And as Mark said, our financial position gives us the flexibility to move very quickly when we see the right kind of opportunity such as is the case with Corob last year.

Andrew Buscaglia - *BNP Paribas - Analyst*

And David, maybe just following on that comment, are the deals you're looking at, is -- are these opportunities where you see some sort of margin potential where you can improve them? Are you mostly after companies that are already fairly fine-tuned? It just get you into the different adjacent market and help you grow from there?

David Lowe - *Graco Inc - Chief Financial Officer, Treasurer*

Well, I think it depends. I mean this is one person's view and we welcome other points of view. I think we have an open mind when we go in. We certainly are interested in those niche market opportunities that have the characteristics of the markets that we're already in. Meeting essential needs for businesspeople, business to business. We like recurring revenue, et cetera. We do understand from our own experience that sometime when we go in and we buy businesses that maybe have been held privately or maybe by a founding family, they haven't always had the capital to inject in the business to bring their plant and equipment up to what I would call the kind of expectations we have for our operations.

And frequently, when we have brought our capital to some of the opportunities that we pursued over the years, powder coating, in the semiconductor space, et cetera, that has represented a real margin improvement opportunity. And so I certainly like that attribute although the underlying businesses were good ones to start with.

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Yeah. I'll just add on that we run DCF models. We're looking to get double digit rates of return for our shareholders. We aren't looking at companies that we can't help them either grow their top line or expand their margins. And so we feel like the businesses that we have acquired, we've got a good track record of being able to do that and that's really what we're targeting.

Operator

There are no further questions. I will now turn the conference over to Mark Sheahan.

Mark Sheahan - *Graco Inc - President, Chief Executive Officer, Director*

Okay. Well, that concludes today's call. I want to thank you for participating and have a good day.

Operator

This concludes our conference for today. Thank you all for participating. Have a nice day. All parties may now disconnect.
