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# EDITED TRANSCRIPT

Q4 2020 Graco Inc Earnings Call

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**Mark W. Sheahan** *Graco Inc. - CFO & Treasurer*

**Patrick J. McHale** *Graco Inc. - President, CEO & Director*

## CONFERENCE CALL PARTICIPANTS

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**Bryan Francis Blair** *Oppenheimer & Co. Inc., Research Division - Director & Senior Analyst*

**Deane Michael Dray** *RBC Capital Markets, Research Division - MD of Multi-Industry & Electrical Equipment & Analyst*

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**Joseph Alfred Ritchie** *Goldman Sachs Group, Inc., Research Division - VP & Lead Multi-Industry Analyst*

**Matt J. Summerville** *D.A. Davidson & Co., Research Division - MD & Senior Analyst*

**Michael Patrick Halloran** *Robert W. Baird & Co. Incorporated, Research Division - Associate Director of Research & Senior Research Analyst*

**Saree Emily Boroditsky** *Jefferies LLC, Research Division - Equity Analyst*

**Walter Scott Liptak** *Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst*

## PRESENTATION

### Operator

Good morning, and welcome to the fourth quarter conference call for Graco Inc. (Operator Instructions)

If you wish to access the replay for this call, you may do so by dialing (855)-859-2056 within the United States or Canada. The dial-in number for international callers is (404)-537-3406. The conference ID number is 5162659. The replay will be available at through 2:00 p.m. Eastern Time, Tuesday, February 2, 2021.

Graco has additional information available in the 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 questions and answers after the opening remarks from management.

During this call, various remarks may be made by management about the 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 indicated as a result of various risk factors, including those identified in Item 1A of the company's 2019 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](http://www.graco.com) and the SEC's website at [www.sec.gov](http://www.sec.gov). Looking-forward 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 the new information or future events.

I will now turn the conference over to Kathy Schoenrock, Executive President, Corporate Controller.

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### **Kathryn L. Schoenrock** *Graco Inc. - Executive VP, Corporate Controller & Principal Accounting Officer*

Good morning. I'm here today with Pat McHale and Mark Sheahan. Our conference call slides have been posted on our website and provide additional information that may be helpful.

Sales totaled \$470 million this quarter, an increase of 14% from the fourth quarter last year and an increase of 12% at consistent translation rates. Net earnings totaled \$115 million for the quarter or \$0.66 per diluted share. After adjusting for the impact of excess tax benefits from stock option exercises, net earnings totaled \$106 million or \$0.61 per diluted share. Gross margin rates increased 130 basis points from last year's fourth quarter. Realized pricing and foreign currency were favorable in the quarter. Mix was also favorable as we saw the margin impact of sales growth in our higher-margin Industrial segment more than offset the continued strength in our lower-margin Contractor segment.

Operating expenses increased \$7 million in the fourth quarter as compared to a year ago due to increases in sales and earnings-based expenses and higher product development costs.

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The reported income tax rate was 11% for the quarter, down 5 percentage points from last year, primarily due to an increase in tax benefits related to stock option exercises. After adjusting for the effect of stock option exercises, our tax rate for the quarter was 18%, slightly lower than the fourth quarter last year due to additional foreign income taxed at lower rates.

Cash flows from operations totaled \$131 million in the fourth quarter and \$394 million for the full year. Discretionary cash outflows in the quarter included the final repayment of \$125 million of the \$250 million borrowed on the revolving credit facility in the first quarter. We also made a voluntary contribution of \$20 million to our U.S. pension plan. For the full year 2020, dividends paid totaled \$117 million, and capital expenditures were \$71 million.

A few comments as we look forward to 2021. Based on current exchange rates and the same volume and mix of products and sales by currency, the effect of exchange is currently expected to benefit sales by 2% and earnings by 6% for the full year, with the most significant impact coming in the first half. Unallocated corporate expenses are projected to be \$30 million and can vary by quarter. The effective tax rate for the year is expected to be 18% to 19%. Capital expenditures are expected to be \$115 million, including \$80 million for facility expansion projects. We may make share repurchases in 2021 via opportunistic open-market transactions or short-dated accelerated share repurchase programs.

Finally, 2021 will be a 53-week year with the extra week occurring in the fourth quarter.

I'll turn the call over to Pat now for further comments.

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### **Patrick J. McHale *Graco Inc. - President, CEO & Director***

Thank you, Kathy. Good morning everyone. All of my comments this morning will be on an organic constant currency basis. The second quarter in a row the Contractor segment exceeded 30% growth and ended the year with record sales and earnings. Contractor grew in all regions during the quarter and for the year. Residential construction activity remains solid, and the home improvement market robust.

Contractor North America saw strong out-the-door sales in both pro paint and home center, and we continue to work hard to maintain adequate channel inventory.

The Industrial segment grew mid-single digits for the quarter but still ended the year, down 10%. Compared to the previous 3 quarters, activity improved in some key end markets like spray foam, electronics and battery. Access to industrial facilities remains limited, but quoting activity has improved. The Asia Pacific region was up versus last year's Q4, which was particularly weak. Price realization, solid factory performance and good expense management, combined with improved sales, resulted in strong Industrial operating earnings for the quarter.

Process segment sales declined 10% for both the quarter and the year. A number of markets in our Process segment remain challenged, particularly those related to the vehicle lubrication or oil and gas sectors. Heading into 2021, we expect challenging end market conditions to remain in place in our Industrial and Process segments for at least the first half of the year as lockdowns persist and access to customers remains limited. Our outlook for the Contractor segment remains positive as favorable conditions continue, and demand has been solid to start the year.

Thanks to our outstanding employees, suppliers and distributor partners, we were able to keep our factories and distribution centers fully operational, avoid layoffs and wage reductions and fully invest in our core long-term growth strategies of new product development, channel expansion and new markets. A special thanks is in order to our Contractor employees and the employees from other factories who relocated to the Contractor factory to assist with a large demand spike in the second half. From the sales team to the shop floor, the Contractor team worked incredibly long hours, maintained a positive attitude and were committed to doing whatever it took to get the job done. Culture matters, and they are winners. We exited the year with momentum and look forward to the fight again this year. Operator, we're ready for questions.

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### **QUESTIONS AND ANSWERS**

**Operator**

(Operator Instructions) Our first question will come from the line of Deane Dray from RBC Capital Markets.

**Deane Michael Dray RBC Capital Markets, Research Division - MD of Multi-Industry & Electrical Equipment & Analyst**

Can we start in Contractor? Just a couple of things. One is, what's the visibility beyond the 6-week average orders that you're giving, which we appreciate. But just what are kind of the data points that you're using, you expect to stay robust? If you have line of sight into that? And then also, you called out some mix issues in the segment. Maybe you can clarify that, too, please.

**Patrick J. McHale Graco Inc. - President, CEO & Director**

So it's a book-and-bill business. So we're always interested every week in what's happening with incoming order rates. However, when you take a look at the macro, residential construction, looks like it's going to remain in pretty good shape through 2021. So we expect to capitalize on that. And at least currently, what we're hearing and what we're seeing, there doesn't appear to be a big pullback in what's happening with the home centers work-from-home business. So we feel like, based upon the orders to start the year and what we're hearing in the marketplace that we've got a good shot of having a successful year in Contractor, despite the fact that we do have some very tough comps that we're going to be up against as we get into the peak that we hit this year.

In terms of the mix issue on Contractor, typically, that's just a mix issue between selling more of the smaller units than the larger units or home center business versus pro paint.

**Deane Michael Dray RBC Capital Markets, Research Division - MD of Multi-Industry & Electrical Equipment & Analyst**

All right. That's helpful. And then just as a follow-up, can you clarify for us on what the opportunity is in batteries? I mean when we talk to our auto analyst, he keeps emphasizing all the growth in batteries and capacity that's coming on new technologies, and just remind us where and how does Graco play in that market?

**Mark W. Sheahan Graco Inc. - CFO & Treasurer**

Yes. Deane, it's Mark. And we play in our Industrial segment in areas where customers are putting in new battery facilities, and they're looking to use fluid compounds to either do bonding of various components of the batteries themselves, or we also get involved in what's called thermal interface materials, which are highly reactive abrasive materials that are put down to dissipate heat when batteries are actually being used. And we have the equipment and the expertise to get involved in those applications, along with our distributor partners to put together nice packages for the end users. So as long as there's demand for batteries, we expect that we're going to get a fair shot at being able to be involved in those opportunities.

**Deane Michael Dray RBC Capital Markets, Research Division - MD of Multi-Industry & Electrical Equipment & Analyst**

Got it. And if I could just squeeze one more question in? Can you talk about pricing expectations? I know it's at the beginning of the year is when you put through pricing. What are the dynamics this year? And anything contribution from new products you expect to launch?

**Patrick J. McHale Graco Inc. - President, CEO & Director**

Yes. Pricing ought to be like it is typically. We generally put through a modest price increase each year and expect to realize somewhere in that 1.5%, maybe up to 2% realized pricing. I don't think this year is going to be really anything different on that. We did not cut any of our new product investments or our new product programs. So we feel like our new product pipeline for '21 and even going into '22 looks pretty good.

**Operator**

Our next question will come from the line of Saree Boroditsky from Jefferies.

**Saree Emily Boroditsky Jefferies LLC, Research Division - Equity Analyst**

We're hearing that there's a lot of capital being spent on automation in China right now. Could you comment on what you're seeing there that drove the pickup in Industrial? And then do you think that COVID will increase the demand for more automation in factories globally?

**Patrick J. McHale Graco Inc. - President, CEO & Director**

So there's a lot of talk about COVID increasing the demand for automation. I think we saw the demand for automation trend. That's been a multiyear trend. That's really nothing new. Well, will it add a little bit of juice to the fire for some folks? I suppose that it probably will.

In terms our Asia Pacific performance, it was good, vis-à-vis 2019, but I would remind you that we did have a pretty weak fourth quarter that we were comparing to. So while business is improving there, we definitely need to see strength globally to get maximum performance out of China because a lot of their work, of course, gets exported.

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**Saree Emily Boroditsky Jefferies LLC, Research Division - Equity Analyst**

Then last quarter, I believe you talked about being surprised if Industrial and Process demand do not kind of move together. The Process does seem to be lagging here. So do you expect the sales there to bounce back as we've seen in Industrial?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

Yes. I would say that I was a little bit surprised, but not terribly because within Process, we've got some segments that have felt more pain than others. And particularly, I referenced the vehicle services and the oil and gas industries. So they're actually taking the average in that Process segment down. And so we need to see some recovery there.

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**Saree Emily Boroditsky Jefferies LLC, Research Division - Equity Analyst**

And then if I could just one last question. Similar to the question on batteries. There's been a lot of talk in the auto industry about the amount of capital needed to support electric vehicle production. Have you looked into what that opportunity means for Graco?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

Yes. A lot of our applications in automotive are going to be the same, whether the car has got gas engine in it, a diesel engine in it or an electric motor in it. We do a lot of seam sealing. We do bonding. We do sound deadening. We do anti-flutter. We do lightweighting activities. Obviously, we do finishing systems. So those necessarily aren't driven by just what's happening with the drivetrain. We're trying to capitalize where we can in markets like battery that Mark gave you a nice summary on. And we don't, today, get a lot of work on the actual drivetrain itself. We don't sell a lot into direct drive manufacturing. So I don't view switch to electric vehicles is being a major change in the business for Graco.

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**Operator**

Our next question will come for line of Mike Halloran from Baird.

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**Michael Patrick Halloran Robert W. Baird & Co. Incorporated, Research Division - Associate Director of Research & Senior Research Analyst**

Just a quick clarification, I think to Deane's last question. So Pat, you're saying price cost positive is still what you guys are angling despite the inflation and still thinking about a more normal price increase?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

Well, I talked about what I thought a realized price increase would be. We are definitely seeing some commodity inflation. And how that's all going to play out? I'm not sure. With some volume, I think our factories are going to perform. So I feel pretty good on the overall cost side, despite the fact that we'll probably get some commodity pressure.

And the other thing that I would point out is that historically, when we see commodity pressure, we have good years of good top line performance. That tends to get a lot of things going that are in our wheelhouse. So while I'd love to have strong top line and commodity is getting weak, typically, we don't see that, and I think it's actually a positive sign.

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**Michael Patrick Halloran Robert W. Baird & Co. Incorporated, Research Division - Associate Director of Research & Senior Research Analyst**

No. That's helpful. And then maybe some context on the Industrial segment. Maybe 2 things here. One, sustainability of the momentum that you saw kind of sequentially through the quarter. And obviously, a little different sequentially on the revenue line versus what the

order trend seems to be. But maybe some thoughts there? And any specifics on end markets, auto, anything else of size that you think is moving the needle one way or another?

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**Mark W. Sheahan *Graco Inc. - CFO & Treasurer***

Yes, Mike, the business tempo in Industrial, obviously, did get better in Q4. But we hope it continues here as we get into the first half of the year. Profitability was way up, as you saw in Q4. Some of that was due to just the fact that we had some lower spending as a result of COVID. I would expect that as our teams get back out on the road and we start re-engaging with customers and moving around that we'll be spending more, and also the incentives for that particular segment haven't been great this year with business being down. So there's going to be a normal uptick in spending. Hopefully, the volume tracks with that. It should. And that we're able to put up decent operating margin performance here in '21.

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**Michael Patrick Halloran *Robert W. Baird & Co. Incorporated, Research Division - Associate Director of Research & Senior Research Analyst***

Helpful. And then last one, I'm sure the answer probably hasn't changed a heck of a lot here. But just thoughts on the M&A environment from your perspective and actionability as you see it today?

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**Patrick J. McHale *Graco Inc. - President, CEO & Director***

It's still expensive. And while we'd like to do something bigger, my guess is what you'll see is niche-type things that we can leverage into either existing businesses or that we think we can build on. And I wouldn't anticipate in this environment that you should bank too much on anything big happening.

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**Operator**

Our next question will come from the line of Bryan Blair from Oppenheimer.

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**Bryan Francis Blair *Oppenheimer & Co. Inc., Research Division - Director & Senior Analyst***

A couple of follow-up questions. And I apologize if I missed some of the detail in prior responses. Starting with the Industrial rebound in Asia Pacific, admittedly versus a weak comp last year. How much of that was driven by automotive lift? And how does that sector momentum, if we're correct in that read, factor into the 6-week booking rates to kick off 2021?

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**Mark W. Sheahan *Graco Inc. - CFO & Treasurer***

Yes, Bryan, we don't break out the automotive portion of the business. It's -- number one, it's really hard to quantify it. We sell-through distribution, and then we don't exactly know where stuff goes. And number two, just for competitive reasons, we don't think it's a good thing to do if we have the data available. So I would characterize it as more of a broad-based recovery across the Industrial product categories. As you mentioned, the comparison was really pretty low for them in Q4. I think, last year, Industrial was down somewhere around 26% or 28% in Q4. So they made a come back. And on a full year basis, Asia is down 1%. But for the full year last year -- Asia was down about 19% last year on a full year basis. So we're encouraged by the momentum that we're seeing. But hopefully, the business continues, the temple stays, and we should see decent year here in 2021.

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**Bryan Francis Blair *Oppenheimer & Co. Inc., Research Division - Director & Senior Analyst***

Got it. Okay. And then on Process trends and in the areas of sustained pressure there. The lubrication business and oil and gas, I guess to address the second first, I believe oil and gas exposure is very modest, following your Alco divestiture. Is that correct? And then with lubrication, I would assume that you have some sequential momentum in there, but perhaps I'm overlooking the timing of spending. Any color would be helpful.

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**Patrick J. McHale *Graco Inc. - President, CEO & Director***

Yes. So we don't break out the sequential momentum by individual product line within a segment that just takes us to no man's land. So I'm not going to go there.

On the oil and gas side, you're correct. Our direct oil and gas exposure is not large. However, indirect oil and gas exposure, it can be

meaningful, meaning that we sell in the industries that are -- also do well when oil and gas does well. So we would like to see some sustainability of the kind of the recent uptick in oil prices. And I think if that can happen over a period of time, we'll see some reinvestment, and that should help us across a number of our business lines.

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**Operator**

And our next question will come from the line of Jeff Hammond from KeyBanc.

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**Jeffrey David Hammond KeyBanc Capital Markets Inc., Research Division - MD & Equity Research Analyst**

Just on Contractor. If you look at kind of the bookings mix and what you're hearing from customers, do you expect kind of the smaller and the home center to continue to be strong in weigh on mix? Or what are you thinking there?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

Yes. It's kind of hard to predict. I mean that's what we've experienced recently. I think that in my time here at Graco, I've never seen anything like we've seen here in the last 6 or 8 months on many fronts. And so we're not trying to predict the future, and we've withdrawn sort of our forward-looking guidance. But what I'm hearing and what I'm seeing, I believe that both the paint channel and the home center channel are likely to remain favorable markets for us as we go through '21 here.

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**Jeffrey David Hammond KeyBanc Capital Markets Inc., Research Division - MD & Equity Research Analyst**

Okay. Great. And then just on the 6-week booking, back on Industrial, is that growth pretty broad-based geographically? Or is that still being driven kind of heavily by the Asia Pac?

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**Mark W. Sheahan Graco Inc. - CFO & Treasurer**

Yes. I think it's more or less broad-based, Jeff. I don't think there's any one particular region that's standing out more than the others.

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**Operator**

And our next question comes from the line of Joe Ritchie from Goldman Sachs.

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**Joseph Alfred Ritchie Goldman Sachs Group, Inc., Research Division - VP & Lead Multi-Industry Analyst**

Pat, maybe just starting off, can you just tell us a little bit about how your parts and accessories business trended throughout the quarter versus maybe like new equipment sales?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

Yes. No, looked right in line with how it always looks, which is not surprising because that's how it always looks. But I think we're fine there.

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**Joseph Alfred Ritchie Goldman Sachs Group, Inc., Research Division - VP & Lead Multi-Industry Analyst**

Okay. So yes, I guess the question is really trying to get a sense for whether maybe like break and fix is trending better than new. But what I'm sensing is basically trending kind of in line with each other. Is that the right way to think about that?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

Yes. And you can go back. It's pretty amazing. And you can go back in time and quarter-by-quarter and year-by-year, and it doesn't vary more than 1 point or 2. So it's really pretty steady. And I think there's more reasons for that than just what's happening at the end market level. You have to keep in mind that we ship our products pretty much same day. We have some products we don't, but the vast majority of our products and order comes in and it gets shipped out.

So what the local distributors need to carry is they need to carry the service and repair parts that are needed to be able to take care of their customers. And so they'll typically carry inventory on service parts and then they'll typically order the larger, more expensive items on an as-needed basis. So I think that kind of has an accumulator effect, a dampening effect on what we see in our parts and accessories business because distributors carry stock.

**Joseph Alfred Ritchie *Goldman Sachs Group, Inc., Research Division - VP & Lead Multi-Industry Analyst***

Got it. Okay. And then maybe just kind of following on maybe just a margin question for Industrial. Like obviously, the incremental margins this quarter were extremely strong. And you guys didn't take a lot of discretionary actions in 2020. So like how should we be thinking about the incremental margin in Industrial in 2021?

**Mark W. Sheahan *Graco Inc. - CFO & Treasurer***

Yes. I'd say, like what we've always said, Joe, if we can get that mid-single-digit or higher top line growth rate, we should be in the -- above 40% incremental margins for that business, that segment.

**Joseph Alfred Ritchie *Goldman Sachs Group, Inc., Research Division - VP & Lead Multi-Industry Analyst***

Okay. Was there -- and was there anything unusual that impacted the fourth quarter? Because you were in that mid-single-digit range, but the incrementals were much stronger than that.

**Mark W. Sheahan *Graco Inc. - CFO & Treasurer***

Yes. I think the biggest -- couple of things I mentioned. One, currency definitely helped on the gross margin line, but also just the absolute level of spending that we had. And the fact that we didn't have as much volume and earnings-based expenses in the P&L in Q4 versus what we would had a year ago, I think those are the major factors.

**Joseph Alfred Ritchie *Goldman Sachs Group, Inc., Research Division - VP & Lead Multi-Industry Analyst***

Got it. Great. If I could maybe sneak one more. The 53-week year, I guess just sales and margin impact, I mean, is it just as simple as thinking like a 2-point impact in sales? And is it any impact to margins from the extra week?

**Patrick J. McHale *Graco Inc. - President, CEO & Director***

I'm going to jump back for a second to your prior question. Just in general, when you're looking at our different segments, looking at incremental margins quarter-to-quarter, I think, is less instructive than looking at them on an annual basis because lots of things can make them jump around. So I think if you're really trying to figure out what's going on at the incremental margins, you'll serve yourself well by looking at the kind of the annual numbers.

On your second question, the 53rd week, that's always a big debate internally here, too. What is that 53rd week worth? Is it worth 2 days? Is it worth 5 days? Which days are they? Are they busy business days? Are they between Christmas and New Year? So I can't give you an actual answer on that. And if you ask 5 business leaders at Graco, you'd probably get 5 little bit different answers. So it's probably somewhere between 1% and 2% on the top line.

**Operator**

And our next question will come from the line of Matt Summerville from D.A. Davidson.

**Matt J. Summerville *D.A. Davidson & Co., Research Division - MD & Senior Analyst***

Just one question here, most of mine have been answered. As we think about -- is there a way to think about how much lack of accessibility to facilities has hindered Graco's top line? And the reason I ask is in the context of, theoretically, this vaccine sort of ramps up, maybe that tempers the accessibility issue for you guys. Can you see some release in pent-up demand? Is there a way you guys are thinking about that?

**Patrick J. McHale *Graco Inc. - President, CEO & Director***

I don't think it's measurable. Meaning, I don't think there's any way we can measure it. Certainly, we believe that not getting our salespeople in front of customers is hurting our top line. We don't get a chance to push the new products. We don't get to be proactive, walking through factories, looking for opportunities to sell something that maybe the customer didn't even know that they wanted. You got a lot of the engineering folks to be working from home, which I think is less effective.

So there's an impact there, but how to measure that, I really have no idea. I think that to the extent that we start to see the world loosen up, we're going to feel better our opportunities, and we should see that in the top line, particularly in the Industrial and potentially the



Process segments. And we're kind of looking towards maybe the back half of '21 to see some more normalization. As you've been watching in the news right now, depending upon where you're looking in the world, there are different levels of loosening and tightening. And it's really hard to predict really one month to the next. So we're going to keep doing our job and do the best we can, but we would really like to have access to customers back to a more normal process.

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**Matt J. Summerville D.A. Davidson & Co., Research Division - MD & Senior Analyst**

At some point, Pat, I guess, what would you need to see in your business? And it's great, by the way, that you give the sales cadence and the 6-week order data. I really like that granularity. At some point, do you think Graco will get back to providing at least at a high level, some sort of guidance framework? And if so, what do you need to see to be able to do that?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

Yes. I think it's likely that we will. I'm not going to promise that we will, but I think it's likely that we will. But we just need to have confidence that what we're telling you has got something behind it. And right anybody who thinks that they can predict what the world is going to look like in 3 or 4 months is probably -- it's probably a coin flip or a swag or whatever. And we try to be a little bit more finite with our guidance than just taking a guess. So we're just going to hold off here. And I think you have to make some macro calls when you take a look at the world and you take a look at what's happening with other industrial companies and what's happened with macro data and what's happening with COVID and try to make some call on your own. Because from our standpoint, it's pretty much of a wildcard.

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**Operator**

And the next call will come from the line of Drew Buscaglia from Berenberg.

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**Andrew Edouard Buscaglia Joh. Berenberg, Gossler & Co. KG, Research Division - Analyst**

I was hoping you could -- can you give us some indication around margin expansion potential in 2021? Because there's a lot of puts and takes and that costs are going up, it seems like you're going to have pricing offsetting some of that, and you're going to face really tough comps in Contractor or even on the margin side. So where -- I guess where is the juice for margin expansion next year -- or this year, rather?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

So I think the positive view is with commodity prices going up, typically, that would indicate that things are going to be good on the Industrial side of our business. And obviously, we've got great incremental margins on the Industrial side. What we saw in 2020 was the Contractor growth really carried the organization lower overall margins. And really pressure on Process, Industrial on the top line, created some challenges for us on operating margin. So I think as you see Industrial and Process pop back, you're going to see those 40%-plus kind of incremental operating margins that are going to drive nice profitability for Graco.

I'd really like to see those in the high single digits, which would not be unusual at all for recovery. We see recovery in the past, getting high-single-digit growth out of our Industrial business has been something that we've seen. I think it's more of a question about when than if I expect it to come back, but I just don't know exactly when. Obviously, signs short-term are looking positive, and we like that. But I think there's still some uncertainty in the next half year or so here.

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**Andrew Edouard Buscaglia Joh. Berenberg, Gossler & Co. KG, Research Division - Analyst**

Yes. Okay. Okay. And your -- and Pat, you're kind of in a pickle with use of cash here because it sounds like M&A is tough valuation-wise. Your stock is not exactly cheap. So you can't really -- a big buyback is probably unlikely. I don't know where you -- how are you thinking about use of cash? And with these -- with M&A -- when you guys be able to find some accretion, just given kind of where your valuation is relative to the companies you're buying?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

So I think one of the keys during times like this is to be patient. We don't have -- I don't have any hair but if I did, it wouldn't be on fire right now because of the amount of cash that we have in the bank. That provides us some nice opportunity to do something. We continue to be active in looking for M&A opportunities. I was just suggesting really that if you're building a model, I wouldn't put it in there. We're not going to go out and do something just because we have a pile of cash. Our shareholders expect us to invest that and get a good

return. And they don't expect us to go and just blow it off the balance sheet immediately on a poor return investment when a little bit of patience could be in order.

So we're going to do like we've always done. And we're going to be opportunistic. If we see opportunities to buy our stock back at what we think are good prices. And we're going to look for M&A opportunities. We're going to invest back in the business in new product development and automation and other cost reduction projects and the Graco program is going to continue. And hopefully, we'll continue to put up results like we have in the past. But yes, I don't feel any urgency on it.

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**Operator**

And our next question will come from the line of Walter Liptak from Seaport Global.

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**Walter Scott Liptak Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst**

I wanted to ask about Industrial. And I guess, it's good to see sort of these early signs of recovery, especially in that 6-week bookings number. I wonder as you look at the data, was there anything that stood out to you like geographically or by industrial sector that you could -- might give us some insight into what's going on in the industrial sectors?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

No. As Mark alluded to on an earlier question, it seems to be spread out, not just all concentrated in 1 spot, right? And again, when you see what's happening with commodities, that would kind of indicate that there's some reason for optimism here. So we'll have to -- we need a little bit longer time before we're going to get bullish on it, but I would say that we feel positive about where we're at versus where we were at 6 months ago.

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**Walter Scott Liptak Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst**

Okay. Is it -- any thoughts about -- is this new capacity that's coming online? Or is it capacity upgrades because of new products?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

Well, the world has been producing. But there's been some interesting dislocations out there in the marketplace. And then there, of course, have been lots of, I'll say, unusual situations just in terms of employees at work and what are they doing? And I feel lucky for Graco as an organization, our engineering groups have remained very active. They've been on-site, they've been getting the job done. We've been investing in capital equipment, buying robots and automation. But certainly, that hasn't been the case. There have been lots of factories where they're hanging in there, and they're doing what they need to do to get by. But they're minimizing the number of resources that they have on the ground and definitely put a damper on Industrial CapEx. So it's very unusual situation, and it's pretty fluid. And I'm not sure exactly what it's going to take to get it back. But I would say that the likelihood that is 6 months' worth of vaccines changes things, at least in key markets in Western Europe and the U.S. seems to be favorable.

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**Walter Scott Liptak Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst**

Okay. Okay. And just thinking about the 6-week orders again. As you look through those, is the timing of shipments stretched out or is this stuff that will go in early in the year for installation?

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**Patrick J. McHale Graco Inc. - President, CEO & Director**

So we have some businesses within Industrial that have run on backlog and longer lead time. But I haven't parsed the 6-week number, so I can't give you an exact thing. But my sense is that it looks pretty much like it typically does.

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**Mark W. Sheahan Graco Inc. - CFO & Treasurer**

Yes. I would just add that the 6 weeks is a pretty short time period. So there's some danger involved in trying to extrapolate those numbers. There's systems jobs in there. There's some lumpiness, both positive and negative. So take it with a grain of salt.

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**Operator**

And if there are no further questions, I will now turn the conference over to Pat McHale.

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**Patrick J. McHale *Graco Inc. - President, CEO & Director***

All right. Well, thanks, everybody, for your participation here today. Thanks to all the employees for the great job that you did in the quarter. And we're going to start 2021 out with a little bit of momentum, and we're going to do our best to have a decent year. So with that, we'll sign off.

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**Operator**

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

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