



Graco Inc. (GGG)

Updated November 5th, 2023, by Patrick Neuwirth

Key Metrics

Current Price:	\$77	5 Year CAGR Estimate:	7.4%	Market Cap:	\$13 B
Fair Value Price:	\$78	5 Year Growth Estimate:	6.0%	Ex-Dividend Date¹:	01/17/24
% Fair Value:	99%	5 Year Valuation Multiple Estimate:	0.2%	Dividend Payment Date¹:	02/02/24
Dividend Yield:	1.2%	5 Year Price Target	\$104	Years Of Dividend Growth:	26
Dividend Risk Score:	A	Retirement Suitability Score:	C	Rating:	Hold

Overview & Current Events

Graco Inc. (GGG) is a manufacturing company, which designs, manufactures, and markets systems and equipment used to move, measure, control, dispense and spray fluid and powder materials. It operates through the following segments: Industrial, Contractor and Process. The Industrial/Automotive unit accounted for 37% of 2022 sales; Contractor, 25%; Process, 25%. 42% of 2022 sales originated from international customers. The \$13 billion company was founded by Russell Gray and Leil Gray in April 1926, is headquartered in Minneapolis, and has about 4,000 employees.

On October 25th, 2023, Graco released its third quarter 2023 results for the period ending September 30th, 2023. For the quarter, the company reported net sales of \$539.7 million, a 1% increase compared to \$545.6 million in the same quarter last year. This result was led by a 9.5% increase in Process segment sales and a 1% increase in Industrial segment sales, while the Contractor segment contracted by 7%. Adjusted net earnings were \$133.1 million for the quarter and adjusted earnings-per-share equaled \$0.77, up 15% and 15%, respectively, compared to \$116.2 million and \$0.67 in the year ago period. Gross profit margin rate was up 5 percentage points from the third quarter last year, mainly due to the realized pricing and lower product costs. Operating earnings expressed as a percentage of sales for the quarter increased 4 percentage points to 30 percent in all three segments.

Graco provided a positive outlook for full-year 2023, as management expects organic revenue growth to be in the low single-digits on a constant currency basis with growth projected in all segments and regions, despite lower Contractor segment volumes and uncertain macroeconomic conditions. This outlook is below the growth figures realized in 2022. Graco expects to launch new products, explore new markets, expand its global channel, and make strategic acquisitions during the period.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS²	\$1.00	\$1.07	\$1.09	\$1.18	\$1.45	\$1.90	\$1.90	\$1.92	\$2.52	\$2.66	\$3.00	\$4.01
DPS	\$0.34	\$0.38	\$0.41	\$0.45	\$0.49	\$0.56	\$0.66	\$0.71	\$0.77	\$0.84	\$0.94	\$1.38
Shares³	183	178	167	168	169	165	167	169	170	169	169	169

Graco's long-term earnings growth track record is strong, with the company's earnings-per-share stabilizing in 2018 and growing thereafter to \$2.52 in 2021. Over the last decade, the average EPS growth rate is 11.5%, which is above the 9.1% rate for this industry.

We expect the company to grow its earnings-per-share by 6% per year on average over the next five years. The company remains well-positioned in its markets and could continue to grow through new product developments, new markets, global expansion, and acquisitions. Supply-chain issues (related to component availability) and logistic problems will be challenging for Graco. Our intermediate-term growth rate is slightly higher than the company's EPS expectations for 2023. The company has a long history of paying dividends and has increased its payout for 26 consecutive years. In December 2022, the quarterly dividend increased by 12% from \$0.21 to \$0.2350 per share. Over the last five years, the

¹ Estimated date

² Diluted earnings; excludes nonrecurring items.

³ In millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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average annual dividend growth rate is 10.9%. Graco repurchased common stocks worth \$27.1 million in the first nine months of 2023.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Avg. P/E	22.3	23.7	21.9	21.9	25.3	23.6	25.2	28.8	30.5	25.0	25.7	26.0
Avg. Yld.	1.9%	1.5%	1.7%	1.7%	1.3%	1.2%	1.4%	1.3%	1.0%	1.3%	1.2%	1.3%

During the past decade shares of Graco Inc. have traded with an average price-to-earnings ratio of about 25 times earnings and today, it stands at 25.7. We are using 26 times earnings as a fair value baseline, implying the potential for a valuation tailwind. Graco's dividend yield is currently 1.2% and the dividend raises in the last few years have contributed modestly to total returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	34%	36%	38%	38%	34%	29%	35%	37%	31%	32%	31%	34%

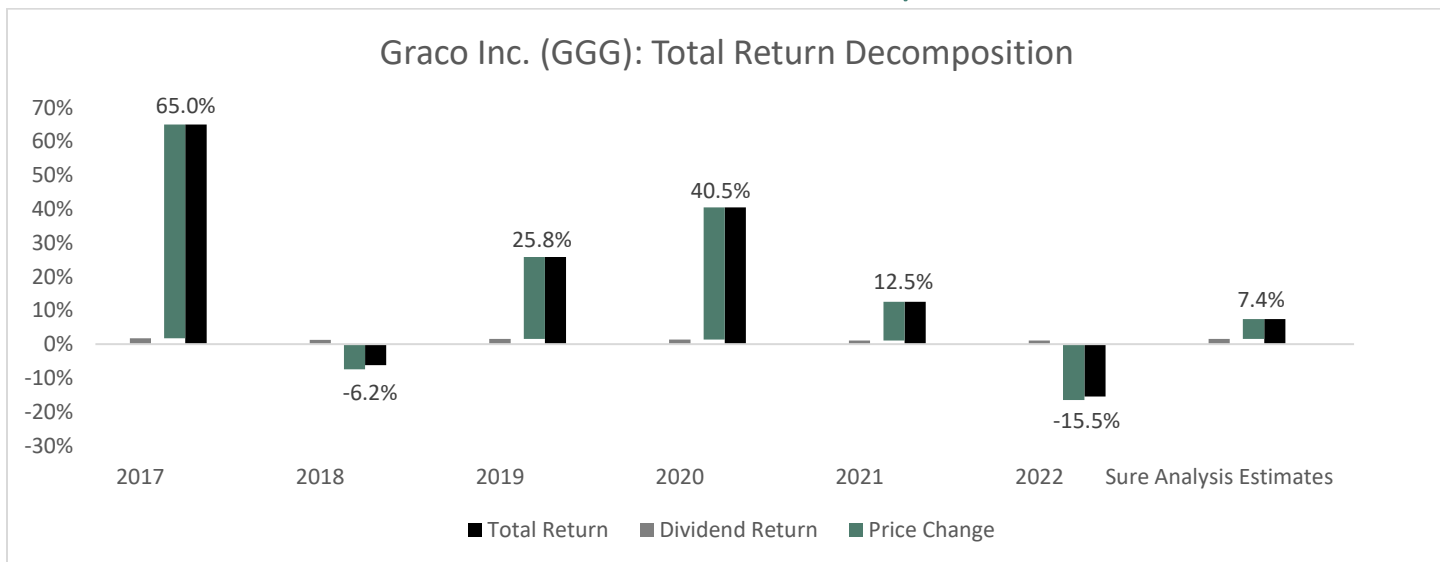
During the past five years, the company's dividend payout ratio has averaged around 33%. The payout ratio is not very high, which makes us believe that the dividend looks quite safe. Given the expected earnings growth, there is still room for the dividend to continue to grow and extend the track record of consecutive dividend increases which is an important factor for dividend growth investors.

Graco's industry is not one with outstanding growth rates, but the company has established itself as a major player that continues to grow profitably year over year. The annual price increases will continue to boost sales and profits. Important elements of Graco's business model are manufacturing excellence, service excellence (same-day delivery) and their extensive reach with 30,000+ outlets/distributors. The company's experienced management and strong fundamentals, such as an above-average return on capital (28%), are also competitive advantages.

Final Thoughts & Recommendation

We expect the company to grow its earnings-per-share by 6% per year on average over the next five years. The expected total returns for Graco are 7.4% per year, driven by earnings growth and a 1.2% dividend yield. We are enthused about the business model and long-term growth potential. Shares earn a hold rating at the moment.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	1,104	1,221	1,286	1,329	1,475	1,653	1,646	1,650	1,988	2,144
Gross Profit	607	667	685	711	795	883	860	855	1,034	1,057
Gross Margin	55.0%	54.6%	53.2%	53.5%	53.9%	53.4%	52.2%	51.8%	52.0%	49.3%
SG&A Exp.	276	304	324	338	357	383	368	356	423	405
D&A Exp.	37	36	45	48	46	48	49	55	59	66
Operating Profit	280	309	302	313	379	436	424	427	531	573
Operating Margin	25.3%	25.3%	23.5%	23.6%	25.7%	26.4%	25.8%	25.9%	26.7%	26.7%
Net Profit	211	226	346	41	252	341	344	330	440	461
Net Margin	19.1%	18.5%	26.9%	3.1%	17.1%	20.6%	20.9%	20.0%	22.1%	21.5%
Free Cash Flow	220	211	150	234	298	314	291	323	323	176
Income Tax	78	90	129	56	95	70	62	44	69	105

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	1,327	1,545	1,391	1,243	1,391	1,473	1,692	1,988	2,443	2,439
Cash & Equivalents	20	24	52	52	104	132	221	379	624	339
Accounts Receivable	183	215	226	218	266	275	267	315	325	346
Inventories	134	160	202	202	239	284	273	286	382	477
Goodwill & Int. Ass.	341	472	625	440	464	463	473	511	508	508
Total Liabilities	693	949	756	669	668	721	667	704	734	579
Accounts Payable	34	39	41	40	49	57	54	58	78	84
Long-Term Debt	418	620	409	315	233	277	172	172	193	96
Shareholder's Equity	634	596	636	574	723	752	1,025	1,284	1,709	1,860
LTD/E Ratio	0.66	1.04	0.64	0.55	0.32	0.37	0.17	0.13	0.11	0.06

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	15.9%	15.7%	23.5%	3.1%	19.2%	23.8%	21.7%	18.0%	19.9%	18.9%
Return on Equity	38.7%	36.7%	56.1%	6.7%	38.9%	46.2%	38.7%	28.6%	29.4%	25.8%
ROIC	20.4%	19.9%	30.6%	4.2%	27.4%	34.4%	30.9%	24.9%	26.2%	23.4%
Shares Out.	183	178	167	168	169	165	167	169	170	173
Revenue/Share	5.86	6.59	7.27	7.78	8.46	9.54	9.59	9.59	11.39	12.40
FCF/Share	1.17	1.14	0.85	1.37	1.71	1.81	1.69	1.88	1.85	1.02

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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