Graco Inc. (GGG)

Updated February 4th, 2024, by Patrick Neuwirth

Key Metrics

Current Price:	$87	**5 Year CAGR Estimate:**	6.4%	**Market Cap:**	$14.8 B
Fair Value Price:	$84	**5 Year Growth Estimate:**	6.0%	**Ex-Dividend Date[1]:**	04/17/24
% Fair Value:	104%	**5 Year Valuation Multiple Estimate:**	-0.8%	**Dividend Payment Date[1]:**	05/02/24
Dividend Yield:	1.2%	**5 Year Price Target**	$112	**Years Of Dividend Growth:**	27
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 34% of 2023 sales; Contractor, 42%; Process, 24%. 40% of 2023 sales originated from international customers. The $14.8 billion company was founded by Russell Gray and Leil Gray in April 1926, is headquartered in Minneapolis, and has about 4,000 employees.

On January 29th, 2024, Graco released its fourth quarter and full year 2023 results for the period ending December 29th, 2023. For the quarter, the company reported net sales of $566.6 million, a 2% increase compared to $550.5 million in the same quarter last year. This growth was driven by solid performance across its Industrial, Process, and Contractor segments, with notable increases of 3% in the Americas, 5% in Europe, the Middle East, and Africa (EMEA), and a decrease of 5% in Asia Pacific sales year over year. The Industrial segment reported a slight increase of 1% in revenues to $192 million, whereas the Process segment revenues grew by 4% to $135.9 million. The Contractor segment saw a 2% rise in revenues to $238.8 million, underscoring the positive impact of new product introductions despite slower economic activity in construction markets. The gross profit margin rate for the fourth quarter improved by approximately 4 percentage points compared to the prior year's fourth quarter, mainly due to realized pricing and lower product costs. Adjusted diluted earnings per share were $0.80 for the quarter, up 10% compared to $0.73 in the year-ago period. For the full year 2023, net sales amounted to $2,195 million, representing a 2% increase from $2,143 million in 2022. The annual diluted earnings per share reached $2.94, an 10.5% improvement from $2.66 in the previous year.

Graco provided a positive outlook for full-year 2024, as management expects organic revenue growth to be in the low single-digits on a constant currency. The company remains focused on its core strategies, including new product introduction, accessing new markets, and targeting strategic acquisitions to enhance shareholder value.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS[2]	$1.07	$1.09	$1.18	$1.45	$1.90	$1.90	$1.92	$2.52	$2.66	$2.94	***$3.10***	***$4.15***
DPS	$0.38	$0.41	$0.45	$0.49	$0.56	$0.66	$0.71	$0.77	$0.84	$0.94	***$1.02***	***$1.50***
Shares[3]	178	167	168	169	165	167	172	175	173	173	***170***	***170***

Graco's long-term earnings growth track record is strong, with the company's earnings-per-share stabilizing in 2018 and growing thereafter to $2.94 in 2023. Over the last decade, the average EPS growth rate is 11.9%, 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

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1 Estimated date

2 Diluted earnings; excludes nonrecurring items.

3 In millions.

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2024. The company has a long history of paying dividends and has increased its payout for 27 consecutive years. In December 2023, the quarterly dividend increased by 8.5% from $0.2350 to $0.2550 per share. Over the last five years, the average annual dividend growth rate is 9.1%. Graco repurchased common stocks worth $102.3 million in 2023.

Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	23.7	21.9	21.9	25.3	23.6	25.2	28.8	30.5	25.0	25.7	***28.1***	***27.0***
Avg. Yld.	1.9%	1.7%	1.7%	1.3%	1.2%	1.4%	1.3%	1.0%	1.3%	1.2%	***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 28.1. We are using 27 times earnings as a fair value baseline, implying the potential for a valuation headwind. 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	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	36%	38%	38%	34%	29%	35%	37%	31%	32%	32%	***33%***	***36%***

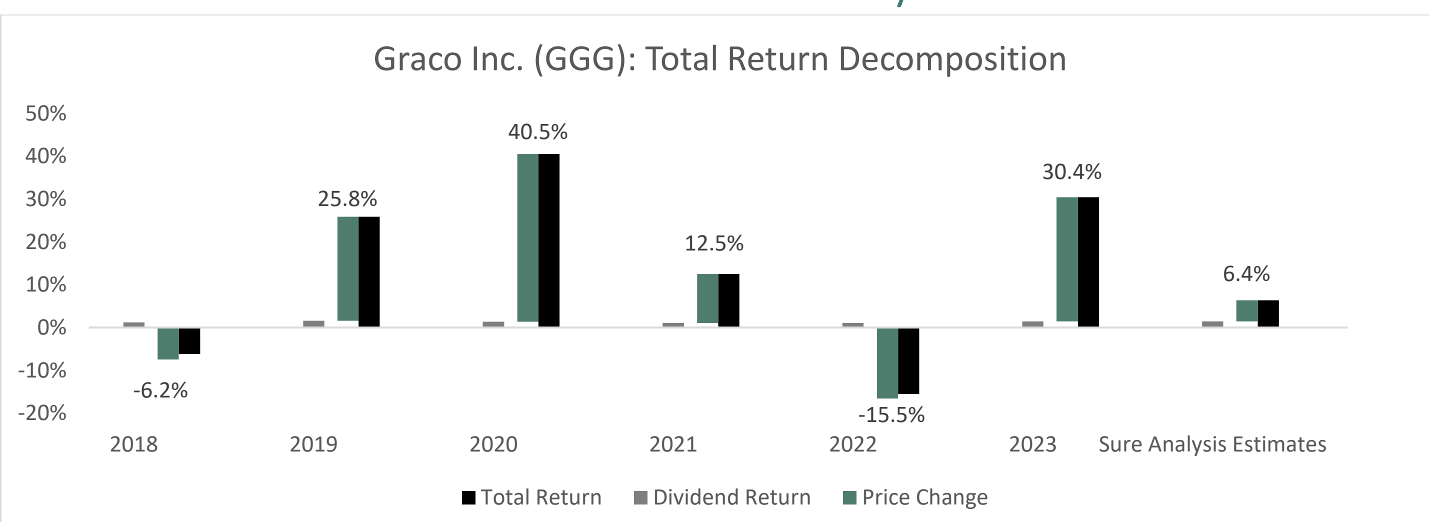
During the past five years, the company's dividend payout ratio has averaged around 33%. The payout ratio is not very high, which makes us believe that the dividend looks quite safe. Given the expected earnings growth, there is still room for the dividend to continue to grow and extend the track record 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 6.4% per year, driven by earnings growth and a 1.2% dividend yield, offset by a valuation headwind. We are enthused about the business model and long-term growth potential. Shares earn a hold rating.

Total Return Breakdown by Year



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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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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.