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The Sherwin-Williams Co. (SHW)

Q4 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

James R. Jaye
Senior Vice President-Investor Relations & Corporate Communications

Q4 HIGHLIGHTS

Performance

- Sherwin-Williams delivered strong fourth quarter results that concluded a record year for the company
- In what remained a very choppy demand environment, full year consolidated sales increased slightly, driven by our deliberate and targeted investments to gain share and overcome softness in core accounts
- Our gross profit, dollars and margin expanded EBITDA dollars and margin expanded and adjusted EPS grew by a near double digit percentage to $11.33 per share
- Consolidated sales in Q4 increased by a low single-digit percentage, and gross margin improved slightly over a very strong level a year ago
- As we expected and previously described y-over-y growth in SG&A moderated to a low single digit level
- Adjusted EPS in the quarter increased by 15.5%

Paint Stores Group

- In terms of our segments in Q4 Paint Stores Group sales increased in the range we expected, led by high single digit growth in Residential Repaint and Protective & Marine
- Consumer Brands Group sales decreased in the range we expected, all related to unfavorable FX as volume and price mix were slightly positive
- Within Performance Coatings Group, sales were slightly below expectations as strength in Packaging and Coil was offset by softness in other divisions
- Adjusted margin expanded y-over-y in all three operating segments
- The slide deck accompanying our press release this morning provides more detail on fourth quarter segment performance
- Let me now turn it over to Heidi, who will provide a few full year 2024 highlights before we move on to our 2025 outlook and your questions

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Heidi G. Petz
President, Chief Executive Officer & Director

BUSINESS HIGHLIGHTS

Opening Remarks

- I hope you had a wonderful holiday season and are geared up for the year ahead
- I know you're eager to get to our 2025 outlook, but first, I want to take a moment to reflect on what our 64,000 dedicated global employees have achieved over the last year
- I am proud of what our team has delivered in 2024

 - We entered the year amidst an extremely choppy demand environment that quite frankly never improved meaningfully
- We knew this was a possible scenario and we doubled down on controlling what we could control

Strategy

- We stayed true to our strategy
- We made targeted investments focused on share gains and executed on our enterprise priorities
- We continued to deliver innovative solutions for our customers and in a disruptive competitive environment Sherwin-Williams stood out by being a consistent, reliable and dependable partner
    - In addition to the strong margin expansion and earnings growth that Jim described a moment ago, it was another very good year of cash generation, which was $3.2B, or 13.7% of sales
- We continued to execute our disciplined approach to capital allocation during the year, including $2.5B, which we returned to shareholders through share repurchases and dividends

CapEx

- In terms of CapEx, we invested $1.1B, including approximately $532mm for our new headquarters and R&D center, which we expect to begin occupying this year
- We ended 2024 with a net debt to adjusted EBITDA ratio of 2.2 times
- Looking at our reportable segments on a full year basis, Paint Stores grew by a low single digit percentage
- Residential Repaint drove the segment growth and increased by a mid single digit percentage
    - This was strong performance given anemic existing home sales and is the clearest example of a return on our prior investment

New Residential and Commercial

- New residential and commercial both increased by low single digit percentages in a challenging rate environment
- Flattish y-over-y segment margin reflects our continued growth investments, which we are confident will continue to drive above-market sales over the long term
- Consumer Brands had a challenging year on the top line, with lower sales resulting from soft DIY demand and unfavorable FX
- Adjusted segment margin expanded back to our target level due to higher fixed cost absorption in the manufacturing and distribution operations within the segment

Investments

- At the same time, we maintained our investments to support our customers, despite weaker-than-expected volume in North America
- Performance Coatings sales varied by division and geography, acquisitions added a low single-digit percentage in the year, but was offset by unfavorable price mix and FX
- Coil was the strongest performer driven by new account wins
- We're also pleased with Packaging, which returned to growth as we won new accounts and recapture the majority of previously lost share just as we indicated we would

Industrial Wood

- Industrial Wood was up mid-single digits, driven by an acquisition
- Accelerated share gains and auto refinish were not enough to overcome softness in core accounts, driven by lower insurance claims
- General Industrial, our largest division, remained under the most pressure during the year, with softness in heavy equipment demand
- Adjusted segment margin expanded to 18%, the highest level since the Valspar acquisition in 2017
    - Throughout 2024, we continued to operate from a position of strength
- In fact, our confidence in our strategy, along with our team's ability to execute, led us to increase several of our midterm financial targets at our Investor Day this past August

Demand Environment

- I am confident we will achieve those targets over time, given a more consistent demand environment
- As we begin 2025, I'm also highly confident that nobody is better positioned than Sherwin-Williams
- During our October earnings call, we were among the first to describe the demand environment as softer for longer, with an expectation that H1 2025 would likely remain choppy
- Three months later, we have seen little evidence to change that view, and given the indicators that we do see several end markets may not improve until 2026

Architectural Side

- On the architectural side of the business, Residential Repaint demand has become slightly more encouraging as existing home sales have begun to show modest signs of recovery and Harvard's LIRA index shows a return to very slight growth
- Residential Repaint remains our single largest share gain opportunity, and we significantly outperformed the market in 2024, given our targeted investments in sales reps, training and digital tools, just to name a few
    - We would expect similar outperformance in 2025
- Looking at new residential, y-over-y growth in single-family starts has been choppy over the last several months, rate cuts have had little impact and mortgage rates remained well above 6%
    - We would expect to continue strengthening our homebuilder customer relationships to outperform the market

Commercial

- In commercial, we've been clear that we expect completions to be soft in 2025 as y-over-y multifamily starts have been mostly down by double-digit percentages since the middle of 2023
- Even if commercial starts do pick up in 2025, which seems unlikely given a consistently soft architectural billing index, they won't turn into painting incompletions until well into 2026
- Property maintenance spending still appears to be idling and neutral
- On the DIY side, we do not currently see a macroeconomic catalyst driving meaningful improvement in consumer demand

Industrial Side

- On the industrial side, the PMI numbers for manufacturing in the US and Europe have been negative for multiple months, with Brazil and China being slightly positive
- We expect Coil to grow again driven by significant new account wins over the past year and a continued focus on new accounts this year
- We're also confident in Packaging growth, as we gain share and support customers conversion to our industry-leading non-BPA coating by 2026 to comply with European Commission mandates

Protective & Marine

- In Protective & Marine, the project pipeline remains solid, though the timing of starts remains variable
- We expect auto refinish demand to remain choppy, driven by continued softness of insurance claims, so our share gains should become more evident
- Industrial Wood will likely track with new residential, given the furniture, flooring and cabinetry end markets that we serve
    - We expect General Industrial demand to remain soft throughout the year

Share Gains

- In summary, the market is not going to give us a lot of help this year
- We'll continue to remain very aggressive with a focus on helping our existing customers grow as well as focusing on targeted share gains
- Against this backdrop, we are providing guidance that we believe is very realistic
- Should the market be better than are currently assuming, we would expect to outperform the guidance we are providing to start the year

Consolidated Sales and Acquisition-Related Amortization Expenses

- Moving on to our specific outlook, the slide deck issued with this morning's press release includes our expectations for consolidated and segment sales for Q1 2025
- The deck also includes our expectations for the full year, where consolidated sales are expected to be up a low single-digit percentage and diluted net income per share is expected to be in the range of $10.70 to $11.10 per share
- Excluding acquisition-related amortization expense of approximately $0.80 per share and restructuring expense of approximately $0.15 per share, adjusted diluted net income per share is expected in the range of $11.65 to $12.05
    - This is a mid-single-digit percent increase at the midpoint compared to 2024's adjusted diluted net income per share of $11.33
- We've provided a GAAP reconciliation in the Reg G table within our press release
- Our slide deck contains several additional data points that provide important context that I'd like to touch on here
- Any comparisons described are y-over-y

Sales Perspective

- From a sales perspective, I'll remind you that the Paint Stores Group implemented a 5% price increase effective January 6

- We would expect this to ramp up to typical 50% to 60% effectiveness over the next quarter
- We also are implementing very targeted price increases in specific areas within our other two reportable segments
- We expect the market asset of raw materials to be up a low single-digit percentage in 2025
- We expect to overcome these raw material headwinds and deliver full year gross margin expansion, driven by incremental 2025 pricing, simplification efforts across our supply chain as well as our Paint Stores Group, which is our largest and highest gross margin segment growing sales faster than the other two segments
- We expect SG&A dollars to grow by a low single-digit percentage in 2025
- This is a more typical level for us and less than last year's 5% increase
    - This year's increase includes $80mm of operating expenses for our new building, which will be weighted to our H2
- We'll also continue to have some operating expense for our current building until we have fully completed our move

Interest Expenses

- As always, we plan to control costs tightly in non-customer-facing functions, and we have a variety of levers that we can pull depending on the material change to our outlook, up or down
- As we've previously described, interest expense will be up this year
    - This increase includes $40mm related to refinancing of debt at higher rates, including $850mm in 2024 and approximately $1B expected to be refinanced in 2025
- It also includes $20mm of interest related to the financing activities of our new buildings

Other General Expense Items

- We expect to end the year within our current long-term target debt-to-EBITDA leverage ratio of 2 to 2.5 times
- Other general expense items are expected to return to more historic levels in 2025 and increase approximately $75mm due to a gain on sale or disposition of assets of approximately $50mm in 2024 that we do not expect to repeat in 2025, and an increase in our environmental provision of $25mm
    - We expect to open 80 to 100 new stores in the US and Canada in 2025
- We'll also be focused on sales rep, capacity and productivity improvements, systems and product innovation

Annual Dividend

- Next month at our board of directors' meeting, we will recommend an annual dividend increase of 10.5% to $3.16 per share, up from $2.86 last year
- If approved, this will mark the 47th consecutive year that we've increased our dividend
- We expect to continue making opportunistic share repurchases
    - We'll also continue to evaluate acquisitions that fit into our strategy
- In addition, our slide deck provides guidance on our expectations for currency exchange, effective tax rate, CapEx, depreciation and amortization

Demand Environment

- Finally, I'll remind you that our first quarter is a seasonally smaller one

- For that reason, we will not be making any updates to full year guidance up or down until our second quarter is completed, and we have a better view of how the paint and coating season is unfolding
- Our team is operating with great confidence and accountability as we begin 2025
- As we have consistently said, it is only a matter of when the demand environment returns to greater strength, not if
- And when that shift occurs, we expect to significantly outperform the market

MARKETS AND SUBSEGMENT

- In the meantime, we are not waiting
- We often talk about how we operate, success by design
- We have a clear and winning strategy
- We have the best team in the industry, and we've made the right investments targeting specific markets and subsegments
    - We know how to deliver solutions for our customers that will make them more productive and more profitable
- We continue to have significant new accounts and share of wallet opportunities in every business and region

SUMMARY

- We expect to continue winning more than our fair share of these opportunities
- I also am highly confident that our enterprise-wide efforts related to talent, simplification, digitization, supply chain responsiveness, and sustainability will continue to deliver above-market growth
- We get rewarded by overcoming obstacles, finding solutions for our customers and delivering results
    - We are extremely well positioned to continue delivering shareholder value, and that's exactly what we intend to do in 2025.

QUESTION AND ANSWER SECTION

Gregory Scott Melich
Evercore ISI

Q

I wanted to follow-up on the raw material expense as part of the guidance expecting that to rise this year. What commodities or areas are driving that? Are tariffs in any way a factor?

James R. Jaye
Senior Vice President-Investor Relations & Corporate Communications

A

Yeah. Good morning, Greg, it's Jim talking. Couple different things to think about there. Yes, there are some tariffs that are embedded in that. Those are tariffs that are already in place, mainly related to Asian imports of epoxy, which came into effect September and November of last year. We're seeing inflation of low single digits in the raw basket. I would tell you that that is related to industrial resins, TiO_2 is up a bit, solvent is up a bit, packaging up a bit.

In addition to that tariff that I described, we have potential for others. Those aren't in the guide right now on the raws, we'll see how that unfolds. I think you have to also think about some other factors, you have suppliers with capacity, rationalization and decommissioning of their plants, which puts pressure on price as well, so we'll see. Natural gas is up as well and trending upwards, which is another pressure point. So I think up-low single digits to start the year and fairly spread out across the year evenly and fairly spread out across the different commodities.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

And Greg, this is Al Mistysyn. The one thing I would add is the additional tariffs that we are tracking very closely that are not in our guidance. If those were to occur and they're significant, we would need to go and we're prepared to go out with additional price in specific markets and segments as required.

Vincent Stephen Andrews
Morgan Stanley & Co. LLC

Q

Could I ask about a couple of the special items that are in the guidance, particularly the $80mm associated with the new headquarters? I know we've talked a lot in the past about the CapEx and the sale leaseback associated with the HQ, but I think this is the first we've talked about there being such a substantial incremental cost to using this new facility. So, I'm just curious if you can help us understand what those are. I don't know, in my head, I would think the new facility would be more efficient from an energy and a water and all that type of thing. So, what's driving the $80mm? And how much of it is onetime in nature vs. nonrecurring?

And then you also have a step-up in the environmental spending and I know that can fluctuate year-to-year. So is there something special about the spend this year that may not recur next year? Or is this a new baseline? Thank you.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah, Vincent. I'll start with the new building. And the way I think about it is this is a transition year for us as a company as we're not moving into – we're going to start occupying the building as the year goes on.

And as we talked about, this is predominantly second-half loaded. I thought I'd be remiss if I didn't include some estimate in our cost base to say that as we get better line of sight on the timing of the occupying the building, we can refine that estimate on our July call. About 20 – I'd say, a-quarter of that $80mm are what I call transition costs, whether that is moving costs, their decommissioning costs related to our old buildings. And yes, they are more efficient.

However, I've got a headquarters building that I've been in for 90 years that is fully depreciated. We've made – I would say we've made measured repairs to the existing building knowing we were going to get out of this building, but if you look at the ongoing service costs, depreciation and things like that, we'll get a better line of sight of that when we're completely into the building, new buildings, we're operating, and we can kind of figure out what's working, what's not working. So these are estimates that need to be refined.

The other comment I would make on the non-operating. Our assumption is we're going to get back to a more normal environmental costs, these are going to be more H1 an impact because we had credits last year. We don't expect to repeat those. I don't think, I would consider it a step-up in environmental provision. I think we've made good progress on remediation and the further we get with remediation, the environmental provisions will get much clearer. So I think it's more of a, back to normal expense in environmental vs. maybe some credits in 2024 that I don't expect to repeat.

David Begleiter
Deutsche Bank Securities, Inc.

Q

Heidi, on the share gain opportunity, can you help frame how that looks to you in terms relative to the PPG business? And looking back to last year, how much of the Kelly-Moore business did you end up picking up? Thank you.

Heidi G. Petz
President, Chief Executive Officer & Director

A

Yeah. Good morning, David. Let me start with Kelly-Moore just because sequentially, obviously, that's, I would say, largely or significantly behind us. I don't know that we shared a number, and I'm certainly not prepared to share a number today, but I would tell you, given how complementary that business model was to us relative to some of the key segments, I'll point to Res Repaint. We were able to, I think, be very well positioned. The team was very aggressive to make sure that we were focused on customer continuity and that we were the house that they wanted to transition to. So we're in a good position there. We expect that to continue into the run rate.

As I look at the PPG sale, I would first describe that as an opportunity that we just came out of our national sales meeting and was able to address over 10,000 of our store managers or reps. And I would tell you, ripe with opportunity is the general sentiment. When you think about breaking that down in terms of how we look at the share gain opportunity, I think you have to start by segment and also a little bit by region, size of contractor. We're largely focused with the crossover between property management, certainly commercial, new residential, so we're going to continue to be very aggressive to make sure that we are best positioned across those segments.

I will also tell you, we are very focused on quality sales and making sure that we're targeting the customers that candidly value what it is that we do and what we bring to bear with our reps, our stores, our delivery, our tools, everything that we can put in front of them to make these contractors even more profitable than they are today is where we're going to focus. But there's a bit of a time lag.

If you think about the speed in which we're able to pick up a Res Repaint contractor, while that's not easy and the team is working very hard to do so. You kind of see that return more quickly vs. someone more in the property maintenance commercial space might be working – will be working on projects that just simply have longer lag periods. There could be bigger sized projects in play that are already committed to. So we're working really hard to really try to sync up as the market does recover, we'll see how the back half of 2025 goes. But as we look into 2026, we want to make sure that we are absolutely best positioned to take that share.

John McNulty
BMO Capital Markets Corp.

Q

So I guess you sounded like there was at least a little bit of optimism in some of the Paint Stores Group end markets, particularly Resi Repaint, I guess can you help us to think about what your customers are saying about their backlog? I know it's a seasonally kind of odd time or early time, but where is that optimism coming from? Can you help us to think about that?

Heidi G. Petz
President, Chief Executive Officer & Director

A

Yeah, John, I'll start here. I think you're right. I mean, we did indicate there's moderate optimism, if I could kind of even moderate the word optimism. We're aggressively partnering with these contractors that are in the current environment, while the market is still choppy. You've seen, I'm sure, certainly the LIRA indicators that paint is likely going to hold up overall over everything else.

But I would tell you, part of this is making sure that our teams are looking to intercept. As you look at our current Res Repaint contractors, our existing contractors, helping them growing their business, helping them market their business, helping them get more leads, close more leads, so that they can become more profitable.

And then in terms of pursuing share gains and new customers, there is a lot of disruption out there, and we are going to continue to be consistent laying in stores, reps, tools, making sure that they're prepared. But I'll hand it over to Al, any additional comments you want to make here relative to some of the indicators?

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah, John. I think I'd just reinforce that we do expect that the demand environment will improve as the year goes on. And I'd highlight that as we've talked about on our third quarter call, as we've talked about on this call, H1 is going to continue to be choppy and a continuation of what we saw in our H2 2024.

Our sales guidance, if you will, for H1 would be up or down low single digits. And then up low to mid-single digits in H2 with our Paint Stores Group being at or above the high end of those ranges.

And you're going to – we do expect some macro improvement as the year goes on, but we also expect to annualize some of the bigger headwinds on our core business that we saw throughout 2024 that we should with the aggressive new account equity and share of wallet activity that each of the teams have completed, we should start seeing more volume as we go into H2. And as you would expect, our earnings will flow in a similar fashion. We expect to be up y-over-y in our H1, but not nearly as much as we do expect to see in our H2.

Chris Parkinson
Wolfe Research LLC

Q

So in addition to some of the gross spend in terms of stores and sales associates, you've also been spending a decent amount on product breadth and some new products and PSG and kind of getting up on some the price points.

And it sounds like you're pretty enthusiastic on some stuff in PC as well. Can I just ask, what are the two to three largest growth or opportunities that you see in 2025 and 2026, when you step back as CEO, just regardless of what the macro environment does, where are you most excited? Thank you.

Heidi G. Petz
President, Chief Executive Officer & Director
A

Yeah, great question. I think there's a number of items, I would point to where we see continued strength. We would expect to outperform Res Repaint, again, I'm going to point to that as an example. You mentioned, how we're looking at product introduction. It's a really good call out because when you think about not only the mix benefit that we see from a margin standpoint, but our ability to bring solutions to these contractors that value productivity above all into the cost of labor being a significant part of the total cost of the job.

We're able to bring technologies. They are more in the premium space, because they are absolutely helping these crews to save time, ultimately money on these job sites. And so there's mix favorability, certainly, which we love because we want to continue to stay kind of cutting edge as leaders and innovating in that space to help these contractors. So that will be the biggest piece.

I think if you look on the performance side, similar to what I mentioned in my prepared remarks as well, I would point to Coil and Packaging as the two, three there. You've got a lot of focus here. Again, the market is not going to help us, but the team has been relentlessly focusing on new accounts, new business wins, fully expect us to continue to do that in both of those segments.

John Roberts
Mizuho Securities USA LLC
Q

Do you expect non-resi to be down all 2025? Or do we have easy comps in the back end of the year where you might actually have some positive comps?

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer
A

Yeah. John, it's possible that we could have positive comps. There's obviously a number of macro things that have to improve to help us, the biggest being as you get into interest rates, and we've talked about proper maintenance and the CapEx shortfalls that we've seen or the lack of investment, I should say that we've seen, we're, again, cautiously optimistic as the year goes on, you'll see some of that improve.

I think commercial, we've been very clear. We do expect to see that drop in our H2, knowing that, we've been really aggressive at pursuing new opportunities to try to mitigate that. As the market goes, we're not immune to that macro slowdown, but we certainly are doing everything we can to mitigate it with these other segments, including P&M and trying to accelerate our Res Repaint to help minimize that.

Joshua Spector
UBS Securities LLC
Q

I wanted to ask on the CapEx guidance. So I mean, a few things there. One, I guess, the $200mm of building spend, is that because the cost of the headquarters is higher? Or are you now doing more or something different there? And then ex that, even the $700mm guide is a bit higher than probably the $500mm that we're modeling longer term. Is there more growth investments that you're doing that is worth calling out now, or is there some reason why your sustainable CapEx should be higher looking two, three years out? Thanks.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer
A

Yeah, Josh. Let me – the new buildings, $200mm is just the combination of finishing up our R&D center in our headquarters. As you know, we will get reimbursed for a portion of the headquarters CapEx in financing, but it all sits in CapEx. And I'm happy to say this will be the last year you'll hear us talk about CapEx for our new buildings.

On the core CapEx, we've targeted 2% of sales. I expect to be in that target long-term. In 2025, we are investing in additional architectural capacity that we've talked about, about our Statesville factory, with our confidence in our long-term growth initiatives within Paint Stores Group, within the Consumer Brands Group we'll fill that capacity up in a fairly short period of time.

And then we're also investing in warehouse automation as we've talked about with labor constrained and manufacturing and distribution, we continue to look for opportunities to automate in those areas to take more weight off the back of our people. So long term, we'll see the benefits of that. But the last thing I'd say is approximately 60% of our CapEx has a return on it and we expect to continue to see efficiencies out of our global supply chain related to that.

Duffy Fischer
Goldman Sachs & Co. LLC
Q

Question on price. So last year, you asked for five in February. This year, you asked for five in January. So can you do the after-action review? How much did you get last year? What was the shape of that kind of throughout the year would be one. Then two, how much of that old price still gets anniversaried this year? And then does the shape of this year's price look different because you asked for it earlier, would you guess?

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer
A

Yeah, Duffy, I think what we talked about on the price last year, let me start with that. It improved as the year went on, and we had talked about coming into our H2 that we'd see a more typical effective rate. So I would say it probably took us longer than we had planned. I would think learning from that, we really led in with a lot of discipline, training in the field, making sure we gave our customers enough lead time to get ahead of it. And I would expect that our effectiveness in price will be better earlier this year than it was last year. It still will take over the next quarter to get to the effectiveness we want. But you'll see a much better effectiveness in our H1 this year than you saw last year. And then the annualization, yes, there's some annualization on the increase last year. And obviously, because we went out earlier this year, we'll see more effectiveness in Q1.

Ghansham Panjabi
Robert W. Baird & Co., Inc.
Q

Heidi, as you kind of think about the six verticals within PSG, has your 2025 outlook changed in any material way vs. your view when you reported Q3 earnings back in October, especially in commercial, maybe?

Heidi G. Petz
President, Chief Executive Officer & Director
A

No, it hasn't. And I think Al characterized that really well just a few minutes ago relative to how we're looking at commercial, in general. If the market does fare better than we're expecting, we expect to outperform the market. But I think this becomes a softer for longer with eyes towards 2026 at this point, Ghansham?

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah, Ghansham, I would just add. I think maybe the rate cuts that the Fed have been doing have not had the effect on the longer-term rates that we were expecting. Mortgage rates are still up in that high 6% range. All things that you're talking nuances related to where we were in October and today, but I think we're in line, if you will, across each of the different segments to say it's +/- a little bit, but we're right in line.

Michael Sison
Wells Fargo Securities LLC

Q

I wanted to get a better feel for maybe some of the headwinds in 2025 in the sense that it doesn't sound like demand is going to be much better in 2025 vs. 2024. Yet in 2024, you generated pretty good EPS growth of 10%. So if you think about 2025, the SG&A increase is going to be a little bit less y-over-y, demand doesn't get much worse. So just curious what else is sort of impeding better EPS growth? And I was maybe hoping your momentum this year would be kind of mirror our guardians, so.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah. I don't know we're going to be that good as the guardians. But yeah, Mike, I think we do have some headwinds additional to what we maybe would have saw in 2024. We tried to call those out, one with higher interest expense with the higher rates. We refinanced the $850mm in Q3 2024 at a higher rate. Our expectation is the $1B we refinance in Q3 2025 will be at a higher rate, plus the financing of our new building is a headwind.

The non-operating costs getting back to a more normal level is a headwind. And we're not hiding behind those, Mike. We saw it coming. We expect that our performance with price, volume, managing our SG&A, to your point, getting on top of the low raw material and other cost basket increases, which y-over-y is going to be a little bit of a headwind.

But I think the incremental new building costs in our H2, so I'm carrying that plus I'm carrying my existing buildings, granted the existing buildings at a lower level, that $0.30 gets you to $12.15 at the midpoint, up about 7%.

So I think that's kind of where we were coming into 2024, and then we saw a little bit better improvement in gross margin. We did manage our SG&A tighter in 2024 than what we had planned, so we got a little bit more of a lift in 2024. And I think coming into 2025, we're in a similar place if you could take out the incremental new building costs.

Heidi G. Petz
President, Chief Executive Officer & Director

A

And Mike, I would add, just from an operating perspective, I think two of the macro headwinds that certainly we're not immune to single-family housing starts have been down y-over-y for three consecutive months and five of that the last eight months. So, we're managing through that.

And then the multifamily housing completes are slowing, given some extended periods of soft start. So there are dynamics that we're going to continue to fight through and compete within them. But I think there's certainly no lack of headwinds as we enter the year.

Jeffrey J. Zekauskas
JPMorgan Securities LLC

Q

Some building products companies have talked about adverse weather, and certainly, it's been cold. When you look at your first quarter, you look at January, is that something that's affected you relative to last year?

And then for Al, in the Consumer Brands Group, the margins for the first three quarters y-over-y relative to last year were up about 10 percentage points, and in the final quarter, they were up maybe 2%. Were there LIFO true-ups or some LIFO dynamic that led to the sort of change in margin differential in Q4?

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah, Jeff, let me start. The cold weather is – we expect that in January. It's our smallest quarter of Q1, I think, where we kind of focus our view is more in our Southeast and Southwest, and yeah, we have more cold there, but I think there's time as we ramp through the quarter to get that back to the – we believe we're within guidance, if you will, right now.

I think when you look at consumer and that's a very good point, that we saw in the first three quarters and talked about the fixed cost absorption adjustments that we made between GS, our global supply chain, which is embedded in our consumer to stores and our Performance Coatings Group to true up those costs. No impact on gross margin. But yes, that impacted the first three quarters. We annualized those adjustments in our fourth quarter. And if you look at our fourth quarter, the increase was primarily due to good cost control, I think that team has done a nice job managing their costs as the year has gone on to tighter volumes.

However, without really sacrificing service and offer options to our customers and partly offset by lower gross profit dollars related to the lower sales, we did still see some benefit in supply chain efficiencies. But going into 2025, our expectation would be those will be incremental improvements because those one-time adjustments, if you will, are no longer happening.

Chuck Cerankosky
Northcoast Research Partners LLC

Q

We've got some very favorable demographic indications for future housing demand. And Heidi and Al, how might you expect it to evolve on the existing home sales and new housing starts without substantial changes in mortgage rates because they just don't seem to suddenly move?

And as you indicated, they haven't been responding to Fed cuts as expected. So what might be the scenarios you see that the housing markets could improve on the supply side? Thank you.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah, Chuck. I think you're absolutely right in the sense that as existing home turnover has been backwards over 36 months in a row, there's pent-up demand that – because household formations continue to be strong, there's still over 1mm, 1.1mm, we've started – life goes on, people get married, people have children, and that just creates more pent-up demand, which may mean – Chuck, which may mean that interest rates don't need to get back to, we were thinking if we'd have to get back to 5% before you start seeing some movement. We saw interest rates drop into that – or 30-year mortgage drop into that 6%, 6.5% range and we saw a nice uptick in existing home turnover.

So I think we might see a different view of the world, a slightly higher interest and mortgage rate gets people to start moving and turning homes more, which would really impact Res Repaint, Industrial Wood, or Coil business on the appliances side and things of that nature. I just think as we've put it out in our guidance, more second-half kind of impacts. It just takes even when an exiting home starts to turn or sale or new residential picks up, it just takes time to filter through to the painting side of that.

Heidi G. Petz
President, Chief Executive Officer & Director
A

And in the meantime, I think what's really important in terms of kind of what we can control in this environment, I'll take you back to the, where we started last year with this, it's when, not if.

In the meantime, as we focus on partnering from an existing home sales, Res Repaint contractors, and I'll take you to our national builders or regional builders on the new res side, making sure that we are partnering with them in new and innovative and creative ways to really help them solve for their biggest pain point, obviously, which is affordability, as we all know.

So I do think that it's masked now because the market hasn't moved, but when the market does move, Chuck, I'm very confident that we're going to be able to demonstrate a different level of partnership with these builders as a result of the team's efforts.

Michael J. Harrison
Seaport Global Securities
Q

We haven't really talked at all about labor costs yet today. I was wondering if you can comment on how changes in immigration policy could impact your business as well as that of your paint contractor customers to the extent that changes in policies could lead to some impacts on labor availability?

Heidi G. Petz
President, Chief Executive Officer & Director
A

Yeah, good morning, Mike. I'd tell you that it's not a new topic for us. I think 150-year-old company, we've certainly seen a lot of administrations. And I do think with what we're seeing here we've been looking at solving for helping our contractors work through some of these challenges that might be – it's too early to tell how this is going to impact the country, let alone our industry and our company.

But I would tell you what's most important for us, regardless of where that does go is we're going to continue to stay laser-focused on helping our customers be productive. And so if I take you to a job site, and you think about a constrained labor, we've got the crew on site.

Our number one job is to get these contractors and applicators on and off the job site as quickly as possible. So, that impacts everything from application to touch-up, avoiding having to come back on the job site. And so the controllables, again, what we are already doing and will continue to do are focusing on the right technologies that help these contractors be efficient.

We are investing, of course, in our delivery and in our service so that we can be accurate and precise in terms of delivery timing, so we're not putting contractors in a position where their crews are idle and waiting.

Certainly, our field reps that we've laid in, this is really critical in terms of problem-solving real-time, contractors having access, again, so that they're not waiting idly and have crews waiting. So, there's a whole host of investments that we've been putting behind this.

Now, if and when and how this impacts us, again, too early to tell, but we're going to make sure that we're best positioned to help our contractors to be prepared and for them to win in this environment.

Michael Leithead
Barclays Capital, Inc.

Q

I just wanted to drill into the Paint Stores' 2025 sales guidance of low to mid-singles, is it fair to think of price at sort of the higher end of that low single digits and then maybe volume probably at the lower end of that low single digits? And then within that volume, is there a meaningful dispersion in your expectations between, say, the five or six different verticals within the segment?

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah, Mike, I think you're correct. I think price will be stronger than volume, especially as you ramp up going through the year. I would say Res Repaint, we'd expect to be at or above the high end of that range, continuing the market share gains and momentum we experienced in H2 2024, which was actually up a high single-digit number.

I think Heidi talked about the other verticals. We do think new res maintains a positive momentum throughout the year. And then I think commercial property maintenance, she touched on both of those. The two, I would also touch on P&M within our Paint Stores Group, I do think up low to mid. And then DIY, I mean, I think is going to be flattish in H1 and then to possibly improve as existing home turnover improves.

Arun Viswanathan
RBC Capital Markets LLC

Q

Just curious, if you think about Q1, obviously, impacted by weather, maybe, do you expect kind of Q2 to Q4 kind of sales growth to be above Q1 levels? And if so, would that be the same for all of the segments or mostly for PSG? Thanks.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yes, Arun. I would say, it's not – I wouldn't point to the weather in our first quarter. Our first quarter is a small quarter. I think it's a continuation of the choppiness we saw in our fourth quarter. And then as the year unfolds, you're going to see varying degrees across the segments.

Let's be clear, Res Repaint, we are very confident, you're going to see consistent mid single-digit growth, if not improving. I think between the other Paint Stores Group segments, I think we just touched on those, that new res, I think is pretty consistent, and the others will improve except for commercial as the year goes on.

I think within our industrial businesses, we're very excited about our Packaging group and the improvements we saw in our fourth quarter and the continuation of that, not to mention the European standard and regulation that goes in H1 2026, so we are going to see customers converting to our non-BPA epoxy, which we believe is first in class.

I think we've talked about auto refinish and our optimism, and we talked about claims being down double digits. I think when you look at North America in our fourth quarter, you're seeing the new account wins that got us into a low single-digit improvement, and we expect that to improve as the year goes on in 2025 as you annualize some of this claims data, you'll see improvement in that area.

Also we've talked about Coil, the new win gains there and that consistency of that team, and that's going to continue in 2025. And then Industrial Wood, we've talked, as new residential improves existing home turnover improves, it really impacts cabinets, flooring, furniture, and the expectation is that improves as the year goes on. I think general industrial has seen the biggest headwinds, they take longer to come out of that, and I'm not expecting that we'll see improvement throughout 2025.

Aleksey Yefremov
KeyBanc Capital Markets, Inc.

Q

Hopefully, sales and demand improve in 2026 or perhaps later. Can you tell us what kind of demand improvement can your current footprint of stores and associates accommodate before you need to ramp up SG&A investments. So would it be 5%, 10% and then you need to ramp SG&A or perhaps a higher number?

Heidi G. Petz
President, Chief Executive Officer & Director

A

I'll start and I'll ask Al to come in. I would tell you we have the capacity. I think the fact that, again, the market is not going to help us, we're out aggressively focused on taking share. We've got the capacity relative to stores.

Having said that, we're going to continue as part of our capital allocation that Al laid out, laying in 80 to 100 new stores throughout the year, and that will be largely focused on geographies where we know we have opportunity to grow and win.

But by and large, I don't know that there's a magic number per se, I mean, our ability to help these contractors to grow is within our capacity, our ability to help our contractors travel from store to store is well within our capacity, so.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah, the only thing I would add to that, Aleksey, think of it as from a rep standpoint, it's a really variable kind of cost that we can ramp up as we see volume improving one to two quarters out with our forecasting models. I think Heidi said it, though, we're adding 80 to 100 stores a year, that gives us great capacity to handle any Res Repaint or other segment increases.

Kevin W. McCarthy
Vertical Research Partners LLC

Q

I have two questions, one for Heidi and one for Al. Maybe to start off with Heidi. On the subject to pricing, I think you mentioned in your prepared remarks, you're pursuing increases in Consumer and Performance Coatings in addition to the Paint Store hikes that we already talked about. How would you – can you elaborate on that? How would you characterize prospects for positive pricing contributions from those two segments in 2025?

And then for Al, what is the level of foreign exchange drag that you're baking into your guide in light of the recent dollar strength? Thank you.

Heidi G. Petz
President, Chief Executive Officer & Director

A

Yeah. Thanks, Kevin. I'll start. The comment that I shared relative to pricing for the segments is that it would be very targeted within the segment. And so you look at that through the lens of regions and geography. Obviously, we're not going to announce here today what those specific actions are, but where we know we need to get price, we're going to be very aggressive and make sure that we do it well.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yes, Kevin, I think on a consolidated basis, FX, we expect to be a headwind of about 1%. But when you really break that out, it's more pronounced in our Latin America teams, in which case, you'll see maybe mid-teens impact on Latin America, which translates to about a mid-single-digit impact on Consumer and then roughly a 2% impact on our Performance Coatings Group.

James R. Jaye
Senior Vice President-Investor Relations & Corporate Communications

A

Kevin, I would just add, you asked about the specific pricing. I'd point out in the slide deck there's a slide that may be very helpful in there that the year breaks out volume price, FX by segment, so you might want to use that as a guide.

Adam Baumgarten
Zelman & Associates

Q

You talked about gross margin expansion in 2025. Can you maybe put a finer point on the magnitude you're anticipating and that's embedded in your guidance? And also, should we think about that as relatively even across the quarters or more H2 weighted?

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah, Adam, we'll not give you an exact number, but you would expect our gross margin expansion to be – let me put it this way, it would be less than it was than we saw in 2024 on a y-over-y basis. As the year progresses, I would expect to see our gross margin get stronger in our H2 vs. our H1 because of the expectation that volume improves.

The price increases are meant to offset raw material cost inflation of the low single digits. Other cost basket increases of low single digits and I'd view that as probably about 75% of the increase. We're also continuing, as we've talked about, self-help initiatives with simplification. We expect acquisition synergies to continue to progress, both sales synergies, but also on cost synergies.

And then we do expect low single-digit production volume increases that with the cost controls that our supply chain teams have put in place that we get some efficiencies out of that and get some small improvements and a tailwind on supply chain efficiencies in 2025. Those wrapped together, probably about a quarter of the improvement.

Garik Shmois
Loop Capital Markets LLC

Q

In Consumer Brands, just wondering if you could speak to how DIY and PRO paint volumes were in Q4? And any color on how you expect them to trend in 2025 would be great.

Heidi G. Petz
President, Chief Executive Officer & Director

A

So, I'll start with DIY. I think we've covered this earlier, certainly weaker than expected. I will share, given from a CBG standpoint, the importance of these customers' strategic partnership that we have, continuing to invest in making sure that we are taking their success and our success, and this is really important that we're laser-focused on ensuring that as the market does recover, that we and they are best positioned on that run-up. In terms of PRO who paints, I'm going to leave that over to Al here.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah. I think the PRO who paints, we are under pressure in our fourth quarter. I think, that being said, we've maintained our investments in the PRO who paints understanding that we don't react to a short-term headwind.

We stay focused on the longer term and fully expect as, think about it, the Paint Stores or – I'm sorry, as the existing home turnover improves, we ought to see PRO who paint improvements in that segment and also DIY improvements in that segment as the year goes on and that's kind of how we laid out the plan from a top line standpoint for Consumer Brands, really similar to how we're looking at Paint Stores Group H1, H2.

Patrick Cunningham
Citigroup Global Markets, Inc.

Q

I'm curious on the latest thoughts on the M&A pipeline. Should we maybe expect less of a focus on M&A this year, given some elevated capital spend, end markets relatively challenging. Any update to your thinking on some of the more sizable coatings businesses that are coming to market?

Heidi G. Petz
President, Chief Executive Officer & Director

A

This is a really consistent approach that we take here, we're always going to be looking. I don't know that I would characterize this as more or less within the year. I think it would be a very steady hand at understanding where our portfolios are, where we want to drive growth within the portfolio by segment.

And if there is opportunity to accelerate our strategy, whether it's a technology, a brand, or a region, we're always looking, but we will go back to our capital allocation policy in general, absent all the items that I'll walk through, we'll look at that, but we absolutely do not need M&A to grow, we're going to continue to focus on putting our foot on the gas where we know we have a right to win today. But should something attractive come along, you can assume that we're going to take a look at that.

Stephen Byrne
BofA Securities, Inc.

Q

I had a follow-up on the labor pool. Just curious whether you're hearing from your Paint Store customers anywhere in the country, in particular, where they're already seeing an impact of the deportation initiative on their labor pool.

And if this is a realistic impact this year, do you think that it might be more impactful on the PRO that paints and maybe shifts more to the Paint Stores business? Or might it shift more to DIY? Any thoughts on that and/or regional impacts in your view?

Heidi G. Petz
President, Chief Executive Officer & Director

A

Steve, I think it's too early to tell. We're not hearing – by and large, we're not hearing, frankly, a lot of commentary about this impacting contractors on the store side or the PRO who paint side relative to their labor pools.

It does certainly reinforce, I think, our position in the market to be able to get ahead of these issues and focus on productivity. I think this just continues to put us in a leadership position there.

In fact, I can tell you, I've been out with over a dozen customers since the start of the year and if there's one theme that's consistent, it's an acknowledgment that you guys are – you're there when you say you're going to be there. Who would have thought simply doing what you say you would do, would be a differentiator?

But the fact that we're staying true to our focus on solving for their profitability and their productivity, I think that positions us very nicely to be able to help, if and when and how this does impact them.

In terms of any kind of toggling or switch between stores and consumer and PRO who paints, I don't see that happening in any material way. I think that that's going to be a dynamic that will impact everybody kind of equally.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah. Steve, the only thing I would add to that, to think that there'd be a shift back to DIY, it's just hard to see that when you look at over a long period of time, the trend from do-it-yourself to do-it-for-me because of some of the macroeconomic situation we have in the US with an aging demographic, the average age of a home in the US is 40 years old, which makes for a more complex type of renovations or projects, there's a lot of equity in homes that allow people to view it as an investment to improve their homes for future value and there's this trend of baby boomers staying in place longer and doing upgrades to their home because they know they're going to be there longer and typically they've got more equity that they can hire out a contractor. So, it's hard to see a flip from back to do-it-yourself over the longer term.

Aron Ceccarelli
Joh. Berenberg, Gossler & Co. KG (United Kingdom)

Q

Perhaps can you elaborate a little bit on the level of profitability of your market share gains? Would it be fair to assume that these new accounts come at least at the beginning at the lower level of margins? Thank you.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah, Aron, I wouldn't classify – I wouldn't make a broad statement like that. I think there's a lot of different activities around new account activation, and depending on where that account is in their maturity level and they may come in from a competitor and want a similar price point until they understand all the benefits, services, quality, delivery, that ecosystem that we talk about, our PRO+ app, and then those are the accounts that we're able to move up because they begin to sense and value what we have to offer. But I would not make a blanket statement, say all new accounts are that way.

Heidi G. Petz
President, Chief Executive Officer & Director
A

In fact, I would go so far as to say, Al made a great point on the maturity of the contractor. Residential Repaint being a great example where oftentimes coming in new, trying to learn, and our teams are able to intercept them early in that maturity curve, even all the way through to helping them present themselves, a professional bid, making sure they've got the yard signed, they're marketing their business, and when they see the value of everything that Al talked about. Our focus then on selling them and putting them into better product and technology, they're going to make them even more efficient, certainly benefits everybody as well.

Eric Bosshard
Cleveland Research Co. LLC
Q

Two things. First of all, I'm curious in terms of price mix, if you're seeing any sensitivity across the architectural business on the PRO side or on the Consumer side, trading down, or anything you're doing in an environment where there's greater price sensitivity. I know that people pay for value and productivity, that's a given with Sherwin. Anything different you're observing or planning for in that area?

Heidi G. Petz
President, Chief Executive Officer & Director
A

No, Eric, I would tell you, if anything, it's the opposite. And you said it really well, the value and productivity, as we continue to launch new products, as we continue to focus on getting our contractors on and off job sites, I think it works, candidly, the other way. And I would say that's true certainly on the PRO side, PRO who paints, and the Consumer side.

Eric Bosshard
Cleveland Research Co. LLC
Q

And then secondly, in terms of the incremental spend on reps and on the selling effort, helpful to see that that spend is moderating a bit in 2025. In terms of the payback, any sense or guidance you can give us in terms of the payback curve as you've added them and invested in them? Are they up at full impact in 2024 [Technical Difficulty] (01:11:05) shows up in 2025? Any thoughts about how you think about the return dynamic from that investment?

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer
A

Yeah, Eric, you kind of broke up, but I think what you're asking is the timeliness of getting a return on our reps. And as you know, they're predominantly Res Repaint reps and I think we get a return on those in one to two quarters, and I think about a density within a market, because what we're able to do in our densest markets is take an existing Res Repaint territory that gets up to a high number of accounts, high level of sales, terrifically successful.

We're able to split that territory, seed some of those accounts that maybe weren't getting the attention that, quite honestly, they deserved. We put a new rep in there, and they both grow quickly back to where they were at a higher level. So the return on a rep, especially Res Repaint rep is really short and we are getting a return, and we expect to see those returns continue into 2025.

Carol Jiang
Jefferies LLC
Q

Maybe just come back to a more general question for the full year 2025. What has to go right for you to hit the high end of the guidance and what might go wrong, given the softer for longer environment? So we look at the lower end of the guidance. Thank you.

Allen Joseph Mistysyn
Senior Vice President-Finance & Chief Financial Officer

A

Yeah. I think where we're going to be within the guidance is going to be dependent on where Paint Stores Group volume is within our high and low end of the range.

And I could say that also about the other segments, but really Paint Stores Group is our fastest growing segment, our most profitable segment, and where they are in that volume range will dictate where we are from an EPS standpoint.

James R. Jaye
Senior Vice President-Investor Relations & Corporate Communications

CLOSING REMARKS

- As we outlined today, we expect the macroeconomic environment to remain choppy in 2025, no surprise there
- But at the same time, and I think Heidi said it very well at the beginning, we're not waiting, we're relentlessly pursuing those opportunities that we do see, it's all about success by design and we have a very proven track record here.
    - We've got a clear and winning strategy, the best team, we've made the right investments, and we know how to deliver the solutions for our customers that are going to make them more productive, more profitable, which is really important in this environment
- Nobody is better positioned than Sherwin-Williams to win in the marketplace and deliver that consistent shareholder value, and that's exactly what we plan to do here in 2025.