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FUL.N - Q4 2024 H.B. Fuller Company Earnings Call

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PRESENTATION

Operator

Good morning, and welcome to H.B. Fuller's fourth quarter and fiscal year 2024 results conference call. (Operator Instructions) As a reminder, this conference call is being recorded. I would now like to turn the call over to Scott Jensen with Investor Relations. Thank you.

Scott Jensen - *H.B. Fuller Company - Investor Relations*

Thank you, operator. Welcome to H.B. Fuller's fourth quarter 2024 Investor Conference Call. Presenting today are Celeste Mastin, President and Chief Executive Officer, and John Corkrean, Executive Vice President, and Chief Financial Officer. After our prepared remarks, we will have a question-and-answer session.

Before we begin, let me remind everyone that our comments today will include references to certain non-GAAP financial measures. These measures are supplemental to the results determined in accordance with GAAP. We believe that these measures are useful to investors in understanding our operating performance and to compare our performance with other companies.

Reconciliations of non-GAAP measures to the nearest GAAP measure are included in our earnings release. Unless otherwise noted, comments about revenue refer to organic revenue and comments about EPS, EBITDA and profit margins refer to adjusted non-GAAP measures.

We will also be making forward-looking statements during this call. These statements are based on current expectations and assumptions that are subject to risks and uncertainties. Actual results could differ materially from these expectations due to factors covered in our earnings release, comments made during this call and the risk factors detailed in our filings with the SEC, all of which are available on our website at investors.hbfuller.com. I will now turn the call over to Celeste Mastin. Celeste?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Thank you, Scott, and welcome, everyone. Overall, I'm proud of the progress we made in fiscal year 2024. We executed on actions to streamline our cost structure and manage the challenging pricing and raw material dynamics as evidenced by the continued expansion of our full year adjusted EBITDA margin.

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We also made significant progress in reducing our net working capital requirements maintaining a stable leverage ratio and enhancing the profile of our portfolio through several strategic acquisitions and the divestiture of our flooring business, resulting in a significant margin uplift. We remain on track to achieve strategic objectives we've laid out for the company.

At the same time, I'm disappointed that we were unable to finish the year as strong as we had expected. In the fourth quarter, we encountered an unexpected deceleration in volume across the majority of our end markets. Furthermore, slowing customer order patterns, particularly in consumer product goods related market segments and our durable goods distribution channel, shifted price increase realization into fiscal 2025, delaying the offset to higher raw material costs and resulting in margin pressure.

We are intensely focused on what we can control and have already begun executing additional pricing actions and cost controls to prudently prepare for a challenging growth environment in 2025. Looking at our consolidated results in the fourth quarter, our organic sales were down slightly, reflecting a weakening economic backdrop.

Volume increased 1.3% year-on-year, while pricing declined 1.5%. Although volumes were still positive year-on-year, the growth was less than anticipated as the portfolio was impacted by a weaker demand environment. The unfavorable impact of pricing continued to be moderate but overall, incremental price realization was below our expectations, particularly in HHC.

Adjusted EBITDA in the fourth quarter was down 14% year-on-year to $148 million, and adjusted EBITDA margin declined year-on-year to 16.1%. The deterioration in margin versus the prior year was driven by unfavorable price and raw material dynamics and higher variable compensation.

Although we did not finish the year as strong as expected, we expanded margins and achieved a new record adjusted EBITDA margin for the fiscal year of 16.6%, keeping us on track to achieve our goal of greater than 20% adjusted EBITDA margin. Now let me move on to review the performance in each of our segments in the fourth quarter.

In HHC, organic revenue was down 2.2% year-on-year, driven by lower pricing and lower volume. Packaging-related end markets exhibited a marked slowdown in volume growth during the fourth quarter as customers delayed orders and overall HHC pricing remain negative year-on-year. Adjusted EBITDA was down year-on-year for HHC in the fourth quarter, and adjusted EBITDA margin decreased year-on-year to 13.9%.

Negative volume leverage the adverse impact from higher raw material costs and delayed pricing drove the margin decrease versus the prior year. In Engineering Adhesives, organic revenue decreased 1.9% in the fourth quarter, driven by both slightly lower pricing and volumes. The Automotive market segment showed continued strength but was more than offset by decelerating durable goods related end markets and slowing distribution channel demand. As expected, solar remained weak during the fourth quarter. Excluding solar, EA delivered positive organic growth in the fourth quarter.

Adjusted EBITDA for EA increased year-on-year in the fourth quarter, the favorable impact from the acquisition of ND Industries was partially offset by lower volume. Adjusted EBITDA margin contracted slightly year-on-year to 19.7%. In Construction Adhesives, organic sales increased 10.5% year-on-year on continued strength in roofing, which grew over 30% year-on-year.

Our performance in construction remains strong as we continue to innovate and expand market share, capitalizing on positive long-term market trends, such as ongoing data center expansion. Adjusted EBITDA for CA increased 12% versus the fourth quarter of last year, driven by strong volume growth.

Adjusted EBITDA margin decreased 30 basis points to 12.3%, reflecting higher variable compensation expense and onetime inventory adjustments. Geographically, Americas organic revenue was down slightly year-on-year in the fourth quarter.

This represents a deterioration versus the third quarter and was driven by significant deceleration in North America volume, which declined from a year-on-year growth rate of approximately 5% in the third quarter to only up slightly in the fourth quarter. Both HHC and EA organic revenue were down modestly versus the prior year, partially offset by continued strong organic growth in CA.

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In EIMEA, organic revenue was down 0.8% year-on-year, driven by slightly lower pricing. HHC organic sales were up low single digits year-on-year, CA was flat, and EA was down modestly. In Asia Pacific, organic revenue was flat year-on-year and continued to be heavily influenced by the solar market segment, which declined approximately 30% year-on-year in the fourth quarter as expected. Excluding the impact of solar organic sales for the Asia Pacific region increased approximately 6% year-on-year, driven by strength in transportation and packaging solutions.

Now I'd like to spend a few minutes discussing a couple of focus areas that support our strategic plan to achieve greater than 20% EBITDA margin. We recently completed a thoughtful and deliberate review of our manufacturing and logistics network and are finalizing a plan to significantly reduce our global manufacturing footprint, streamline our North American logistics and delivery operations and strategically improve inventory management.

This multiyear plan will reduce the number of manufacturing facilities from 82 at the end of fiscal 2024 to a target of 55 by 2030. We have also completed a redesign of our North American logistics and warehousing structure that will reduce the number of warehouses from 55 today to approximately 10 by 2027. These actions will not only reduce costs through improved capacity utilization, they will also enable us to reduce future capital expenditure requirements and better serve our customers.

As a result of these actions, we expect to generate approximately $75 million in annualized cost savings once the plan is complete. These actions will be implemented over the next five years, and we expect to invest approximately $150 million of incremental capital over this time.

We expect the savings to be minimal in 2025, but to ramp significantly in 2026 through 2030. These actions are incremental to the previously announced restructuring already underway which is on track and still expected to generate approximately $45 million in annualized cost savings by the end of fiscal 2025 versus fiscal 2022 with $37 million already achieved through the end of fiscal 2024.

On the M&A front, we recently announced the acquisitions of two leading medical adhesive companies GEM Srl and Medifill Ltd. GEM Srl based in Italy is a market-leading provider of medical adhesives and innovative application devices approved and certified for over 80 internal indications. Medifill Ltd based in Ireland, specializes in formulating and producing medical-grade cyanoacrylate adhesives specifically tailored for the wound closure market.

These highly complementary acquisitions will enhance our market-leading position in cyanoacrylate and expand our market presence in the highly advanced and rapidly growing tissue adhesives market. The transactions represent two significant milestones in the expansion of our medical adhesive's portfolio, a key strategic priority for the company and build on our previous acquisitions of Cyberbond, Tissue Seal and Adhezion Biomedical.

The two companies generated 2024 net revenue of approximately $24 million and adjusted EBITDA of $12 million. On a combined basis, these acquisitions will be completed at a pre-synergy EBITDA multiple of 15.5 times and a projected three-year post-synergy EBITDA multiple of 9.5 times based on a combined purchase price of EUR180 million.

Consistent with our next level portfolio management strategy, we also recently divested our flooring business. The decision to pursue strategic alternatives for this business came as a result of a robust strategic review in both historical and forward-looking financial assessments. As a result of the strategic review, we determined it was unlikely we would achieve our minimum EBITDA margin threshold of 15% for this market segment on a time line and at a level of investment that was acceptable to us.

This move is consistent with our strategy to drive our portfolio focus and capital allocation to the highest margin, fastest growing market segments in this $80 billion global adhesives industry. Concurrent with the flooring divestiture, we also announced the reorganization of our Building and Construction segments into a newly named Global Business Unit Building Adhesive Solutions or BAS, replacing H.B. Fuller's existing Construction Adhesives GBU starting in fiscal year 2025.

The reorganization combines the company's insulated glass, woodworking and composite segments previously included in Engineering Adhesives, with the remaining roofing and building envelope and infrastructure market segments historically included in Construction Adhesives. The

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reorganization into BAS creates a faster-growing solutions business with a more complementary customer base across the architectural and infrastructure markets.

These organizational improvements allow for more effective spec setting in the architectural space and streamline our execution playbook. In addition, it consolidates the more cyclical and seasonal construction-related markets into one GBU, allowing for greater external transparency.

On a pro forma basis, BAS generated approximately $850 million in sales and $120 million in adjusted EBITDA in fiscal year 2024. Our proactive portfolio management strategy is a key part of delivering long-term financial targets and tuck-in acquisitions are an important part of that. Our 2023 and 2024 collections of acquisitions are performing exceptionally well, and we have executed successfully to our synergy targets, even exceeding our business case commitments.

This success provides us with the confidence to continue pursuing strategic acquisitions to further expand our growth market segment mix and improve our overall business profile. We wanted to share some of the financial results from our 2023 collection of acquisitions.

We now have a full year of results for these six deals, which closed throughout 2023. Collectively, these deals delivered approximately $37 million of adjusted EBITDA in 2024, exceeding the collective acquisition case by approximately 10%. We grew 2024 adjusted EBITDA nearly 90% year-on-year versus full year 2023 by successfully executing our synergy plan. These six deals represent approximately $15 million of acquired EBITDA at a purchase price of $216 million and a collective pre-synergy multiple of 15 times. At the time of purchase, EBITDA margin was collectively 8%.

Through the first full year of ownership, the post-synergy multiple has been reduced to less than 6 times and the EBITDA margin expanded to 21%. Per the collective business case, we expect to achieve a combined EBITDA margin of 24% and a post-synergy EBITDA multiple of 4 times by fiscal 2026 for this 2023 collection.

In 2024, we closed two acquisitions. ND Industries and HS Butyl. Both are performing very well and on track with the business case in the 2024 partial year. As a reminder, we acquired $27 million of EBITDA at a purchase price of $275 million and a pre-synergy multiple of 10 times.

We expect to convert this into $47 million of EBITDA by 2027, equating to a post-synergy multiple of less than 6 times. We plan to provide a more detailed update on these two deals this time next year, consistent with what we discussed on the 2023 collection.

The net impact from the annualization of the two deals we closed in fiscal 2024, the two medical adhesive acquisitions that were announced in early December and the divestiture of the flooring business is expected to deliver an approximately 70 basis point adjusted EBITDA margin uplift in 2025. Now let me turn the call over to John Corkrean to review our fourth quarter results in more detail and our outlook for 2025.

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

Thank you, Celeste. I'll begin with some additional financial details on the fourth quarter. For the quarter, revenue was up 2.3% versus the same period last year. Currency and acquisitions collectively had a positive impact of 2.5%. Adjusting for those items, organic revenue was down 0.2% driven by lower pricing.

Volume was up 1.3%, reflecting slightly negative volumes in HHC and EA partially offset by a continuation of the strong growth in Construction Adhesives. Adjusted gross profit margin was 29.6%, down 170 basis points versus last year, driven by a delayed price realization and unfavorable raw material cost developments.

Adjusted selling, general and administrative expense was up 12% year-on-year driven primarily by wage inflation, higher variable compensation expense and the impact of acquisitions, partially offset by our continued cost reduction efforts. Adjusted EBITDA for the quarter of $148 million was down 14% versus last year, reflecting the negative impact of pricing and raw material cost actions, primarily in HHC as well as higher variable compensation expense. The decline was partially offset by the positive impact of acquisitions, continued restructuring savings and other cost reduction actions.

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Adjusted earnings per share of $0.92 was down versus the fourth quarter of 2023 and primarily driven by a decline in operating income. Cash flow was strong for the full year, although lower than we expected, driven by lower operating income. Full year cash flow from operations of $301 million was down year-on-year, reflecting lower operating profit, partially offset by improved working capital efficiency. Net working capital as a percentage of annualized net revenue declined 160 basis points year-on-year to 14.5%. As a result, our net debt-to-EBITDA ratio of 3.1 times was flat versus the end of Q3.

With that, let me now turn to our guidance for the 2025 fiscal year. We anticipate full year net revenue to be down 2% to 4% versus 2024. And when adjusting for the divestiture of the flooring business, to be up between 1% and 2%. Organic revenue is expected to be flat to up 2%. We expect foreign currency translation to negatively impact revenue by about 2% and acquisitions and divestitures to also unfavorably impact revenue by about 2% versus fiscal 2024.

We expect adjusted EBITDA to be between $600 million and $625 million representing a 1% to 5% year-on-year increase as pricing actions, restructuring savings and the impact of acquisitions more than offset variable compensation rebuild and unfavorable exchange. On a constant currency basis, this guidance range represents year-on-year adjusted EBITDA growth of 3% to 7%.

We expect our 2025 core tax rate to be between 26% and 27% compared to our 2024 core tax rate of 26.7%. We expect full year interest expense to be between $120 million and $125 million, depreciation and amortization to be between $170 million and $180 million and the average diluted share count to be between 57 million and 57.5 million shares. These assumptions result in full year adjusted earnings per share in the range of $3.90 to $4.20, representing year-on-year growth of 2% to 9% versus fiscal 2024.

Finally, we expect full year operating cash flow to be between $300 million and $325 million before approximately $160 million of capital expenditures which includes approximately $40 million of capital related to the company's global footprint improvement initiative. Based on the seasonality of our business and the timing of working capital needs, we expect operating cash flow to be weighted to the second half of the year.

Taking into account the current global operating environment as well as the typical seasonality of our business, we expect first quarter revenue to be down low to mid-single digits, reflecting a slower operating environment and the divestiture of the flooring business and for adjusted EBITDA to be between $105 million and $115 million. Now let me turn the call back over to Celeste.

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Thank you, John. I would like to take this time to acknowledge and thank all our employees for their dedication and hard work during the year. Despite significant obstacles in the second half of the year, your efforts enabled us to make meaningful progress on many of our strategic initiatives. As we look ahead to 2025, we remain committed to our portfolio improvement strategy and remain dedicated to the long-term strategic plan we have outlined.

While we are currently facing some near-term market weakness, we are taking all necessary actions to manage costs appropriately, implement our planned pricing initiatives and navigate this period efficiently and effectively. We are confident in our ability to permanently transform this business into a sustainably faster-growing higher-margin enterprise, and we remain on track to achieve an EBITDA margin of greater than 20% on the timeline we originally communicated.

That concludes our prepared remarks for today. Operator, please open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Kevin McCarthy, Vertical Research Partners.

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Kevin McCarthy - *Vertical Research Partners LLC - Analyst*

So last, you've unveiled a fairly ambitious restructuring plan here. I did have a few questions around that. Can you speak to the cash cost to implement the plan that would hit your financials in 2025 and then elaborate also on the flow-through of the expected savings. I think you indicated it may be modest this year and then ramping into 2026, but I appreciate any thoughts on the millions of dollars that will be in the plan?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Sure. Absolutely, Kevin. And yes, it is an aggressive plan. I think it's also a very achievable plan. So, as we captured -- as we outlined that plan in the press release, we talked about the cost savings available to us by so executing.

But when you think about it from a big picture, we've got a big global footprint. And within that footprint, there is redundancy in some technology production in some regions. But there's also opportunities for us to grow capacity for some technology regions where we may not have enough where we may not be able to grow in an end market as fast as we would like. So, as we took a step back and really evaluated that footprint, there are a few things that really triggered for me that we -- it was the right time for us to pursue this project. I mean, first of all, we now have the tools and the diagnostics we need to evaluate the footprint.

I'm also very confident in our operational leadership. They are -- we have the right team in place there. They have good plans in place. They understand the target and they're starting to march forward. One of the ways I tested the team just to ensure we were really ready for such an ambitious goal was to pilot a few location closures.

So in fact, if you look at the Beardow Adams, acquisition. In fact, there are two facilities in Europe and one facility in the US that we closed within 12 months, a very ambitious target that was achieved. So, the team is ready to move forward on this, we're announcing a targeted 27% reduction in facilities. The reality is by the end of 2025, 16 of those will already be complete.

So I am including in '25, the 16 reductions, six from the flooring business we sold, I'm including those three Beardow Adams facilities that we already captured in our synergy numbers. There's a couple of plants that were already in our earlier announced restructuring. So, this $75 million is all additive and we will be -- we have taken some -- we'll have a lot of tailwind, I'll say, in the first stage of the program to reduce from 82 by 16 by the end of '25. John, do you want to talk about exactly how that schedule in over time?

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

Sure. So, I would say it's still a little bit of a work in progress, Kevin, but for 2025, the savings should be roughly $5 million. That's on top of another $8 million related to the restructuring we announced in 2023. So, we'll complete that. This would be an incremental $5 million probably in 2025.

I think that number steps up to closer to $20 million in 2026. And then I would say it's kind of pro rata over the next three years to get to the $75 million run rate. In terms of cost to implement, so in the press release, we talked about the capital costs. We were silent on sort of the other cash costs. Again, that's still being developed.

I would anticipate we'll have some in 2025, but it won't be significant. And over the course of that program, this footprint realignment, it's, again, still estimating it. I'm going to guess it's going to be between $25 million and $50 million of noncapital cash costs. We will have proceeds associated with the sale of these facilities we're exiting. Again, very hard to exit. It may not completely cover the cash cost, but it will cover a significant portion, I would say.

And then capital, we said in the press release, $150 million of capital over the next five years, still an estimate that's being refined. But for 2025, we will have about $40 million in our capital spend, specifically related to the footprint reset. So, I hope -- does that answer your questions, Kevin?

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Kevin McCarthy - *Vertical Research Partners LLC - Analyst*

Yes. That's very helpful. And secondly if I may, I wanted to talk about pricing, maybe a two-part question. In the fourth quarter, I think you indicated that some pricing was delayed, particularly in the HHC segment. So, I was wondering if you could elaborate on what's going on there?

And then the second part would be what is the level of price that you're prospectively baking into your organic sales growth forecast of 0% to 2% for fiscal '25?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Yes. So, let's talk about HHC. So, in HHC, in particular, we saw some significant raw material cost increases really flow through the P&L in Q4 starting in Q3. The team had identified price increases to address that. As volume was lower than anticipated in the fourth quarter, we didn't get that full price realization in place in Q4.

So there's significant increases that they will have -- that they're putting in place in Q1. You asked about the level of price anticipated for 2025, call it sort of 0% to 2% increase in price with volume down mostly across the total business in 2025.

Operator

Ghansham Panjabi, Baird.

Ghansham Panjabi - *Robert W. Baird & Co. Incorporated. - Analyst*

I just want to go back to Kevin's question on the manufacturing footprint optimization and if you kind of zoom out, is the poor of the strategy to kind of build bigger, more productive plants, particularly across the leverage portion of the portfolio? I know, Celeste, talked about 16 plans or so coming out of the system in fiscal year '25, but also just your overview in terms of how you're managing execution risk and customer service throughout this process because it is obviously a very significant initiative.

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Yes, absolutely. So, if you look at, again, the program there's definitely an opportunity for us to put in capacity that capitalizes on some growth markets, but there are a number of cases where we can reduce redundancy. And certainly, for the HHC business, we're looking very, very hard at how do we continue to reduce their overall cost of production they have more leverage market segments in their portfolio than the other businesses.

So absolutely, we want to make sure that we are driving to an optimal cost profile in those businesses. And in some cases, our cost to produce in HHC is just too high. So, they will be the primary beneficiary of this global footprint reduction activity. There's some greenfield activity, Ghansham, but overall, more most broadly, we're really working on consolidating within the existing footprint.

Ghansham Panjabi - *Robert W. Baird & Co. Incorporated. - Analyst*

Got it. And then going back to the fourth quarter, I think this was the first just looking at my model, first year-over-year decline in EBITDA margin since 4Q of fiscal year '22. And I'm still trying to reconcile that because your volumes were up, your pricing was down, but it wasn't worse than in 3Q. So why were margins down so much at over 300 basis points? And also, maybe a corollary question as it relates to volumes for the first quarter of fiscal year '25, how that's tracking relative to what you saw in 4Q?

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Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

So margins were down primarily in Q4 because of the raw material cost flow through that we experienced. I don't know if you remember, like over the last several quarters, we've pointed out that in the first half of the year, we would have tailwinds on raw material and price that comes of that bucket. And again, price was negative because we were overcoming a lot of index pricing issues.

But in the second half, raw materials became a headwind. And as we pointed out last quarter, we anticipated a $20 million increase in raw material costs in Q4. We did experience that, and we experienced all of that in HHC. So that was the primary driver of down margins in the quarter.

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

Yes, Ghansham, your question about what are we seeing so far in Q1. And we only have one month, so it's a small sample size. I'd say they're modestly better, but you also have to remember, Q1 is always our lowest margin quarter, right? The volumes in Q1 because of the Christmas and New Year's holidays, Chinese New Year, are probably on average, we'll probably have $100 million less revenue in Q1 than we will have in any other quarter in the year. But I'd say they're modestly better.

I'd say some of the actions we're taking on pricing, we'll see a little bit of that impact in Q1 but probably more in Q2. Around raws, raw material -- underlying raw material costs are pretty stable from Q4 to Q1. I think our sourcing team has been doing a good job of going out and finding alternative sources of supply.

And they have taken some actions that reduce the impact of what we saw in Q4. But again, because of the timing when they buy materials when they actually work their way through our cost of goods, it's probably more of a Q2 issue.

So I'd say they're holding in, if not a little bit better, and we're taking -- and we see the underlying actions that will help them improve sequentially in Q2.

Operator

Mike Harrison, Seaport Research Partners.

Mike Harrison - *Seaport Global Securities LLC - Analyst*

Appreciate the details on the acquisition progress that you've made with the deals you've done. That's great to hear. I wanted to dig in a little bit more on the HHC business. You called out packaging and consumer. We tend to think of those areas as being a little bit more defensive in nature, and I think packaging had been kind of a bright spot for you earlier in the year.

Can you talk a little bit about what's changed and what drove some of the weakness in those markets? To what extent are we may be seeing some customer inventory rationalization going on? And I guess, how have those trends progressed as we went from kind of November into December and now into January?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Yes. Q4, Mike, was very -- was, I'd call it, a dramatic slowdown in the HHC business, ultimately in consumer-packaged goods. In fact, in Q4, we saw a deceleration in 10 out of our 13 HHC market segments. So, things really slow down there, could be some inventory rationalization at customers, that's a possibility. The other thing we see is even in the distribution business in the packaging arena, our distributors are very cautious, they have seen a significant slowdown.

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I think a lot of share is shifting within consumer-packaged good customers. So, it's been a very, very weak market. The one -- when you look at the market segments that are actually accelerating, it's because of share gains. So, one example would be our flexible packaging business. That's one of our top 20 growth priorities.

Our team there has been able to take business away from competitors that have had it for 20 years with some customers. And so that's a really exciting growth potential for us. That was one of the businesses that was accelerating. And actually, when you look at that, that's fully driven by innovation. That was catalyzed by our ability to solve customer problems where they want to be able to use the same product here that passes European regulatory requirements, for example, and required reformulating on our part to be able to meet needs like that.

So had it not been for our innovation and market share gains in flexible packaging, it probably wouldn't have been a lot different, the market is likely decelerating there as well. So broad-based deceleration in the consumer-packaged goods space.

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

And Mike, just on your question on what we're seeing so far. Again, we just have P1. I would say that the packaging space remains soft. As Celeste alluded to, we knew last year, in the first three quarters, we were kind of outgrowing the market. So, we do have tougher comparisons there.

Hygiene has actually shown some growth in P1, which is positive. Now they have easier comparisons. And then we talked about this deceleration mostly being HHC. There was a little bit in Engineering Adhesives in the durable goods distribution area. And that's actually come back nicely in P1.

So I would say the three areas we saw softness, packaging is -- continues to show softness. Hygiene and other consumer packaged goods are kind of improving a little bit as is durable goods distribution.

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

So this is -- as we look at HHC serious actions underway there to be able to perform effectively in 2025, regardless of what kind of volume the market has to offer. The team's got aggressive price increase plans, they're adding on to their cost reduction plans. And as I mentioned, even longer term, our global footprint rationalization will benefit HHC more than the other business units. And again, we've redirected resources and focus within that business unit onto the higher returning market segment.

So flexible packaging being one of those, but also, you've seen our success in the medical adhesives market and our focus there. Those are the kind of things that we're doing to try to return HHC to the kind of margins and growth rate that, that business should have.

In Q4 of '23, we were comparing to a 19.9% EBITDA margin. We said at that time, that's not likely the go-forward rate. This was 600 basis points less. This is also not the go-forward rate. This is a business that should be operating around 16% EBITDA margin, and the team is taking actions to make sure that happens.

Mike Harrison - *Seaport Global Securities LLC - Analyst*

All right. And just a follow-up on that. You mentioned that the share shift that may be going on among consumer-packaged goods customers, is that leading you guys to potentially lose some market share? Or can you talk about those dynamics a little bit?

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Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

We work with a variety and many customers in cases where the consumer is switching down to lower quality, lower cost products, there can be share shifts as a consequence that include -- that influence us negatively. We tend to work with the more customers that are very interested in innovation and the value the solutions we provide. So, it's a tougher market for that at this point.

Mike Harrison - *Seaport Global Securities LLC - Analyst*

All right. Understood. And then last one for me. If I look -- this is a question on guidance. If I look back over the last couple of years, you came in towards the lower end of your guidance range in fiscal '23. You missed fairly substantially here in fiscal '24 for reasons that we've been talking about here. But can you talk about, Celeste, whether you have baked in some conservatism into your initial 2025 outlook?

And I guess, aside from end market demand what are some of the levers or key factors that are going to help determine whether you can deliver within the guidance range?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Yes. We're committed to delivering within the guidance range, Mike. I mean if you think about what are the opportunities that could impact the business in '25. Here, we're going into 2025, anticipating a slightly negative volume growth environment. So, we want to make sure that we are prepared and that we're doing the things now that need to happen should that volume in this market continue to be weak and sluggish.

So that's what we're anticipating in 2025, and that's what we're planning for. But there are opportunities to grow certainly beyond what we've indicated, I mean, any kind of volume is going to be beneficial in 2025 since we don't have any baked in. We also don't -- we don't have any interest rate cuts included in our outlook.

Again, those would -- should they happen, should probably favorably affect volume, but also will affect our interest rate expense. We may say, if it's a really slow, really poor volume environment, we're going to push towards greater raw material savings. So, we've indicated that the price raw material bucket would be favorable by about $55 million.

There is an opportunity for us to do better there if volume is worse. And we've added to our cost reduction programs. We can add further to those if we see the year not playing out like we believe it will.

Operator

Jeff Zekauskas, JPMorgan.

Jeff Zekauskas - *J.P. Morgan Securities LLC - Analyst*

I think you spent about $275 million for acquisitions in '24. How much do you think you might spend in '25?

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

Well, Jeff, we have spent year-to-date already EUR180 million on our two medical adhesive businesses, as you know. Now if you take into account that we also divested the flooring business in 2025, we're sitting at about $100 million. Our pipeline continues to be robust. There are some wonderful opportunities. We see there the good news about a proprietary deal pipeline, the kind that we -- kind that we participate in that we're growing is that we have a little more flexibility around timing with a pipeline like that.

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So as we've said from the start, our allocation for M&A tends to be in the $250 million to $300 million range. So, you can count on additional M&A happening in 2025 beyond what we've done and announced so far.

Jeff Zekauskas - *J.P. Morgan Securities LLC - Analyst*

Okay. All right. You talked about some raw material inflation. I think the acetic acid are down, propylene is down, polyethylene is down. What went up?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Yes. So, in our HHC business, in particular, which is where most of the raw material increase was centered, we saw some increases in as oil, but most notably in hydrogenated hydrocarbon resins. More as a function of a consumption tax that was not necessarily put in place in China, but that was now being reinforced in China, that's where the impact was. I mean it's not only the resin impact.

Obviously, we monitor 4,000 raw materials. About a quarter of those actually, Jeff, were inflationary. If you look at it on an account basis, but I'm pointing to a couple that were the more significant on a dollar basis inflationary and a unique situation.

Jeff Zekauskas - *J.P. Morgan Securities LLC - Analyst*

Yes. You talked about weakness in packaging at the very end of the quarter. Is that food packaging? Or what's the packaging end market that seems to have softened in a more pronounced way?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

So as you know, we participate in all kinds of packaging applications. So, but most notably, I'd say it's the packaging applications that are sort of case in carton seal more at the end of the line when the customers taking the goods they've produced and boxing them up in order to ship them out. That's where -- now we've also -- we see it across the board, though, Jeff, really, I mean, like you'll see it in tapes, in corrugated a lot of the other different applications in packaging where we participate. It's fair to say they were similarly down.

Jeff Zekauskas - *J.P. Morgan Securities LLC - Analyst*

And then just as John doesn't feel neglected, there was some $36 million outflow in deferred taxes. Is that ongoing? And sort of what's that about?

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

Yes. It was mostly related to a China dividend, a large kind of dividend we took in 2024. And so that was accrued for in 2023, but we pulled the cash back in 2024, something on the order of $100 million came back and there's withholding tax associated with that. So that's more of a onetime item.

Jeff Zekauskas - *J.P. Morgan Securities LLC - Analyst*

Okay. So that number should go down in '25?

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John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

Yes. So I'd say if you look at our tax impacts between the -- withholding tax impact, we did have a few some timing on other payments in 2025, some audit settlements, some timing on our European taxes that made that number probably $20 million to $30 million higher than run rate, and we anticipated that, but that should be more less unfavorable next year.

Jeff Zekauskas - *J.P. Morgan Securities LLC - Analyst*

I guess lastly you're bringing down your warehouses to 10 in the US over time. How many warehouses do you have in Europe?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

That's the -- we can talk about that on another call, Jeff. Let me get through the -- let me get from 55 to 10 in the US first. And really, that shift in the US logistics structure. We're in the process of adding tools and capabilities to allow us to more efficiently manage inventory, to manage transportation. And yes, I mean, 55 warehouses being reduced to 10 is a significant challenge.

That's largely driven by a model shift, so we're going to be moving more toward a DC model in the US. And we're testing these concepts, these new systems, and tools out in the US as and assuming they will be successful, then we can redeploy them to other regions. So, I think it's fair to assume that in Europe, we probably have a lot of warehouses also.

Operator

David Begleiter, Deutsche Bank.

David Begleiter - *Deutsche Bank Securities Inc. - Analyst*

Celeste, in Engineering Adhesives, can you talk to what's driving the forecast of lower volumes? And how much low volumes are you forecasting in that segment in '25?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

As far as forecasting for -- do you want to talk about the forecasting in 2025? (multiple speakers)

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

Sure. So, I think just to kind of frame it, David. So, our outlook on revenue, as we talked about is organic revenue to be flat to up 2%. We've reflected slightly positive pricing, up maybe 1%, 2% and slightly negative volume down low single digits. If we think about how that looks by GBU, we are projecting that Engineering Adhesives will be flattish next year and that HHC will be down low single digits and BAS up kind of low to mid-single digits.

So from a volume standpoint, and pricing in all three will be up kind of 1% to 2%, probably up 1%-ish in EA and 1%-ish in BAS up a little more in HHC. So, volume, as I said, kind of down low single digits in HHC, flattish in EA and up low single digits in BAS. Is that what you were looking for?

David Begleiter - *Deutsche Bank Securities Inc. - Analyst*

Very helpful. And EA, given the macro forecast to call for growth this year, you had a pretty severe volume decline in '23, which you only partially got back to. So why are in volumes up and EA in '25?

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Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Well if you -- let's talk about some of the positive trends there. So, one of the big factors will be that we will wrap around on the solar volumes, right? So those started declining in Q2 that will start to improve in the second half of this year. Also, we've been successful in winning in many of these EA markets. We've grown our electronics business double digits, I mean, 20%, 30% kind of rates depending on which quarter we're talking about.

So a lot of positivity there. And even though there's a lot of macro concerns over the automotive industry, we are growing the automotive space like crazy. And that's really a function of our innovation and ability to expand beyond being the interior trim leader in automotive exterior trim applications and even to the powertrain.

In fact, we just took some business by introducing a highly thermally conductive silicon product for EV powertrains and stuff like acrylic-based structural adhesives that bond spoilers on to the back of the cars and the area of exterior trim. You have to be very fast curing, high stress application and actually very humidity interestingly enough, taking business in the head lamp space automotive. So, there are some markets where you would say, oh, that doesn't sound like it should be a market that would foster growth. But in our case, we were able to grow despite the market underpinnings.

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

And David, I would say we may be being a bit conservative around EA. I think the -- as we said, we're projecting negative volume growth primarily from HHC and then EA flat. It started off stronger than that. I think some of the things we're baking into our assumptions is that although our auto team has done a terrific job winning new business, the macro trends aren't good there. So, we're expecting that to be slower.

Clean energy, as Celeste said, we'll start to annualize against some of that negative performance we saw in the second half, but it will still be a headwind in the first half of the year. But the other markets, electronics, durable assembly, as I said, has bounced back nicely. So hopefully, we're conservative. I think the team is setting higher targets than what we outlined. But there are a few macro headwinds that we're trying to reflect in our outlook.

David Begleiter - *Deutsche Bank Securities Inc. - Analyst*

Understood. And just a good segue to HHC. The guidance of down I guess, 2% to 3% of volumes in 2025, given the rapid deceleration in Q4, I would have thought we would see volume growth in '25. What else is underpinning that forecast of down 2%, 3%, 4% volumes in '25 in HHC.

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Well, it's predominantly the packaging business remaining weak, and we're seeing that still today. So that's had a big effect now. Of course, a lot of our HHC business is in Europe. Europe is just broadly not a growth region. And there's -- overall, I think the consumer-packaged goods space is one that is -- it's hard to predict going into the upcoming year.

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

The other thing I'd say, David, is we're going to be more aggressive on pricing. As we discussed, HHC. I think to get back to the margins we need them to get back. It's really where most of the pricing activity is going to have to happen and may get some volume attrition from that, and that's okay. So we've kind of reflected that in our assumptions as well.

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Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

We match this space, David, where if volumes in any region or globally are really weak, which is what we saw in recall 2023, we saw volume down 10% across this portfolio, that's where we have the opportunity to push much harder on our suppliers and mitigate some of the EBITDA impact there should we actually get into a position like that.

Operator

Patrick Cunningham, Citigroup.

Patrick Cunningham - *Citi Investment Research (US) - Analyst*

I want to retry sort of the price cost question here. I guess, first, I'm curious on how large of an impact whether it's to HHC or the whole business, how large raw material inflation was in 4Q and what impacts expected in 1Q. And I also thought a decent portion of the price decline throughout the year were either index-based contracts or reformulation pressure where it's generally margin dollar preserving.

So I guess, why have you been able to -- unable to pass that through? And how confident should we be that you can push price in HHC for 2025 in this depressed volume environment?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

The index price, remember, Patrick, the indexed pricing does lag three to six months. So, we've seen now this increase in raw material cost the indexes will reflect that next year. So that's one component of this. Yes, reformulation is ongoing for customers, particularly in a low volume environment. And also, in Q4, our teams were very successful renegotiating multiyear contracts with very large customers that will be volume enhancing.

So now that -- depending on the year, you'll see that maybe two years, three years out, depending on what the overall market environment is for volume. But from a share perspective, the team did a very good job on those contracts. Some of that did have an impact on price in Q4. So yes, and yes, a large impact of raws in Q4, when we look at the price raw material bucket for 2025. We're anticipating about a $55 million benefit to EBITDA next -- in this upcoming 2025 year. Do you want to add to that, John?

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

Yes, just in terms of the impact in Q4, Patrick, I'd say it was probably $10 million unfavorable to Q3, which was largely unanticipated going into the quarter, we expected the raws to be pretty flat sequentially. And so that was really what drove that margin compression, particularly in HHC.

And then Q1, we would expect them to be flat sequentially to Q4, and that's what we're seeing so far. There is some expectation we might see some improvement in Q2 based on some actions we are taking around changing sources of the supply and other things. And we should also see the pricing actions we're taking in Q1 really show up much more in Q2.

Patrick Cunningham - *Citi Investment Research (US) - Analyst*

Very helpful. And then construction stood out as being particularly strong in 2025. How would you characterize the strong top line and margin performance? Was it data centers, share gains? Or is it simply just lapping destocking? And then market growth in 2025 doesn't seem to be a given at this point. Why should volumes be up across the Building segment?

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Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

So in our roofing business in particular, which was the primary driver of CA as it has been reported, there's a few positive things happening there. One is first of all, introduction of innovative products. For example, our PG-1 EF ECO sprayable adhesive product took share. The other thing that happened in this current year is we added a business with a large customer. So, we've shifted share from a large customer across the board there. So that had a big influence.

And finally, we are playing in the right segments of the construction market, that data center build, for example, we don't see that abating anytime soon. So, we're playing in the right spaces in construction. I do think the construction market should continue to be strong for us because of those things that occurred in 2024, they'll reoccur in 2025. But yes, we are now annualizing against tougher comps from 2024.

John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

The other thing, I guess, just to remember is this is a little bit different portfolio than it was in 2024 as well in the sense that we now have wood, glass and composites, which did not see the same type of positive macro trends around data centers and other things that we saw in the broader construction market or in roofing in particular. So that's another reason we would expect it to be a little bit slower in 2025.

Operator

Rosemarie Morbelli, Gabelli Funds.

Rosemarie J. Morbelli - *Gabelli & Company - Analyst*

Celeste, I was wondering how soon you knew that fourth quarter was going to be below expectation. What was a surprise from? And is there anything that you are doing currently in order to better manage expectations, for example? Can you help us in all of the different steps, actions you are taking, if anything is addressing that?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Yes, absolutely. So, we knew Q4 was going to be challenging in advance of Q4 in HHC in particular. We moved to put price increases in place not quickly enough. It took too long for those to root in given the lower volume we experienced at the same time during that quarter. So, what are we doing about it?

Because this is obviously top of our list, Rosemarie. We are aggressively revalidating our cost reduction efforts that have been already underway there. Those have been added to by the GBU leader. The pricing actions that we already had in flight have been increased and enhanced. So, you should see better pricing performance from that business given the increase in raw materials.

Our sourcing team has already reallocated business for some of these key HHC raw materials to other suppliers as a consequence of the cost increases, we were seeing from the Chinese consumption tax coming out of Asia. So, it's all hands-on deck, Rosemarie, not just longer-term plans like the global footprint reduction, which will benefit the business, but also immediate actions that we're taking to address it.

And we have immediate actions similarly underway in the CA business. The CA margin was about 300 basis points lower than it should have been this quarter. We had some onetime issues there that the team is addressing and they as well are on top of pricing actions and cost reduction to improve the portfolio.

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John Corkrean - *H.B. Fuller Company - Executive Vice President, Chief Financial Officer*

And just in terms of -- just you had asked sort of about what we -- what was the -- when do we become aware, how do we manage the potential for these things and avoid surprises. So, it was -- the impact in Q4 was definitely weighted to the second half of the quarter, right? So, if you looked at the results, our P10 was very good. Capital as we continued -- it kept us on track for delivering on our expectations. It was really weakening in late October into November.

Some of the markets where we've seen softness coming into the quarter, Clean Energy as an example, was down in Q4 pretty significantly, but in line with our expectations. So, we were able to anticipate that. We weren't able to anticipate the weakness in the packaging and consumer products goods space just because it happened sort of in the middle to the latter part of the quarter.

Rosemarie J. Morbelli - *Gabelli & Company - Analyst*

Okay. That is very helpful. Thank you. And I was just wondering, looking at HHC. Are there additional divestitures of the product lines or any specific categories that you think you should exit in order to get to your 20% EBITDA margin?

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Divesting anything out of this portfolio is very challenging. And again, because our plants, while they're assigned to a GBU, they really are technology-based. And we have such raw material scale that we get benefits from that across the portfolio. Flooring was very unique in that not being the case that was part of the reason why we divested. So rather than looking for divestitures in the HHC space, we're very focused on how do we grow that portfolio in higher-margin, faster-growing market segments.

I talked about flexible packaging. That's an area where we're certainly focused and where the team has done a fantastic job growing the business and doing so profitably. But also in the medical space, that's an area where our HHC resources are being directed toward growth.

And we had really an exciting win just recently, Rosemarie, where our SecurePortIV product was actually not only approved for use in Phoenix Children's Hospital. By the way, it's in use now in 10 of the top 10 children's hospitals in America, but also at Phoenix Children's Hospital, they approved SecurePortIV for not just applications in the central IV catheter space, which is about 10% of that business, but they approved it for every catheter IV catheter application there in the facility.

So we're really seeing growth in higher margin, much more profitable faster-growing spaces even in this HHC business where the medical business resides.

Operator

We have no further questions. I would like to turn the call back over to Celeste Mastin for closing remarks.

Celeste Mastin - *H.B. Fuller Company - President, Chief Executive Officer, Director*

Thank you very much for joining us today. We look forward to updating you on the business during the next quarter. Have a good day.

Operator

This concludes today's conference call. Thank you for your participation. You may now disconnect.

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