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Earnings Call

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Presentation

Operator

Ladies and gentlemen, thank you for standing by. Good day, and welcome to the WD-40 Company Third Quarter Fiscal Year 2024 Earnings Conference Call. Today's call is being recorded. [Operator Instructions]

I would now like to turn the presentation over to the host for today's call, Wendy Kelley, Vice President, Stakeholder and Investor Engagement. Please proceed.

Wendy D. Kelley
Director of Investor Relations & Corporate Communications

Thank you. Good afternoon, and thanks to everyone for joining us today. On our call today are WD-40 Company's President and Chief Executive Officer, Steve Brass; and Vice President and Chief Financial Officer, Sara Hyzer.

In addition to the financial information presented on today's call, we encourage investors to review our earnings presentation, earnings press release and Form 10-Q for the period ending May 31, 2024. These documents are available on our Investor Relations website at investor.wd40company.com. A replay and transcript of today's call will also be made available shortly after this call.

On today's call, we will discuss certain non-GAAP measures. The descriptions and reconciliations of these non-GAAP measures are available in our SEC filings as well as the earnings documents posted on our Investor Relations website.

As a reminder, today's call includes forward-looking statements about our expectations for the company's future performance. Actual results could differ materially. The company's expectations, beliefs and projections are expressed in good faith, but there can be no assurance that they will be achieved or accomplished. Please refer to the risk factors detailed in our SEC filings for further discussion.

Finally, for anyone listening to a webcast replay or reviewing a written transcript of this call, please note that all information presented is current only as of today's date, July 10, 2024. The company disclaims any duty or obligation to update any forward-looking information as a result of new information, future events or otherwise.

With that, I'd now like to turn the call over to Steve.

Steven A. Brass
CEO, President & Director

Thank you, Wendy, and thanks to all of you for joining us this afternoon. Today, I'll provide you with an overview of our sales results for the third fiscal quarter of 2024, an update on our Must-Win Battles and progress we've made on certain strategic enablers. After that, Sara will provide you a brief update on the divestiture of our home care and cleaning business, an update on our business model and an outlook for the remainder of fiscal year 2024. We'll then take your questions.

I'm happy to share with you that for the third consecutive quarter, we saw sales growth across all 3 of our trade blocks. Today, we reported net sales of $155 million, an increase of over 9% and a new record quarter for the company. Excluding the favorable impact of currency, revenue grew 8%. In addition, sales of maintenance products grew over 10% for both the third quarter and year-to-date, which is in line with our long-term growth targets.

We remain encouraged that the improvement in trends we experienced in the first half of fiscal year 2024 have carried into the third quarter. Sales volumes continue to improve. And in the third quarter, nearly all our sales growth was driven by volume with currency and price impacts nearly canceling one another out. In addition, we're pleased to report that gross margin continues to improve and is moving closer to our long-term target of 55%. In the third quarter, we reported gross margin of 53.1%, which is an improvement of 70 basis points sequentially and 250 basis points compared to the third quarter of last

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fiscal year. Driving improvements to gross margin enables us to invest in critical areas of our business like our Four-by-Four Strategic Framework, which will help us to continue to drive faster top line growth and improve operational efficiencies.

Now let me discuss third quarter sales results by segment. Unless otherwise noted, I will discuss sales on a reported basis and compare to the third quarter of last fiscal year. Sales in the Americas, which includes the United States, Latin America and Canada, grew approximately 6% over the prior year to $75.1 million. The bulk of this growth was driven by higher sales of WD-40 Multi-Use Product which increased 7% compared to the prior year. Much of this growth came from strong sales of WD-40 Multi-Use Product in Latin America, which increased by 51% year-over-year. These increased sales were partially offset by lower sales of WD-40 Multi-Use Product in the United States and Canada.

Our Latin America market is comprised of our direct markets in Mexico and Brazil, and all remaining Latin American countries, most of which are served by marketing distributor partners in the region. Sales in Latin America was favorably impacted by our transition to a direct market model in Brazil.

Early in the third quarter of fiscal year 2024, we acquired our Brazilian distributor and shifted from an indirect distribution model to one where we sell directly to retail customers. This distribution model shift favorably impacted net sales in Brazil by $2.7 million in the third quarter.

In addition, sales in Mexico and other Latin American markets increased $2.8 million due to the timing of customer orders, successful brand building programs, increased distribution of WD-40 Smart Straw and favorable impacts of changes in foreign currency exchange rates.

While end user demand remained relatively constant in the United States, sales decreased by 2% compared to the prior year quarter. This relatively flat performance in the U.S. was driven by several factors. Firstly, we're lapping an extremely strong U.S. performance in our FY '23 where the U.S. experienced exceptionally strong volume recovery post price increases and grew by 17%. We also experienced strong declines in our long strategic [household] brands in the U.S., which decreased in Q3 by 15%. Our combined maintenance product sales in the U.S. for Q3 declined by 2% whereas year-to-date, they have grown by 2%, and we expect modest growth for the full year.

Our ERP implementation did not have a material impact on our U.S. results in the third quarter, whereas we continue to experience some disruption, this lessened as the quarter progressed to the extent that by the end of the quarter, we were approaching traditional customer service levels with order fill rates and on-time and in-full delivery also referred to as OTIF deliveries well into the 90% level.

Our plan for FY '24 in the Americas was always driven primarily by strong Latin American growth and that is playing out. Sales of WD-40 Multi-Use Product in Canada decreased 13% period-over-period due to phasing associated with the discontinuation of our classic can delivery system and the implementation and conversion of Smart Straw in Canada. We have taken some short-term pain in Canada to drive a very significant long-term gain as we fully leverage our Smart Straw and EZ-REACH formats.

In the Americas, sales of WD-40 Specialist increased across most regions and were up 10% compared to the prior year, primarily due to new distribution, the timing of customer orders in the United States. In total, our Americas segment made up 49% of our global business in the third quarter.

Turning to our sales results at EIMEA, which includes Europe, India, the Middle East and Africa. Sales in EIMEA grew approximately 13% over the prior year to $59.4 million. Currency fluctuation has positively impacted our sales in EIMEA and a constant currency basis, sales would have increased 10%. The growth was driven in large part by higher sales of WD-40 Multi-Use Product which increased 17% and WD-40 Specialist, which increased 11%.

As a reminder, volumes last year were unfavorably impacted by price increases we'd implemented, resulting in temporarily reduced demand as customers adjusted to these prices. The combination of recovering volumes and increased selling prices resulted in higher sales across most regions in EIMEA this quarter. In the third quarter, we saw double-digit growth of WD-40 Multi-Use Product in nearly all our EIMEA direct markets with particularly strong growth in France and Italy, which increased $1.4 million and $1.2 million, respectively.

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In our EIMEA distributor markets, sales were up 14%, primarily due to recovering volumes and increased selling prices, resulting in higher sales across most regions. Sales of WD-40 Specialist increased across most regions of EIMEA and were up 11% compared to the prior year due to the combined impact of higher sales volume due to increased distribution and stronger levels of demand after customers adjusted to price increases. The growth in maintenance products was partly offset by a decline of 19% in home care and cleaning product brands, which are not a strategic focus for us and are expected to decline due to our shift in focus on core operations during the ongoing sales process. In total, our EIMEA segment made up 38% of our global business in the third quarter.

Turning to Asia Pacific, which includes Australia, China and other countries in the Asia region, Sales in Asia Pacific grew approximately 14% over the prior year to $20.5 million. The growth was driven by higher sales of WD-40 Multi-Use Product, which were up 11%, higher sales of WD-40 Specialist, which were up 30% and higher sales of home care and cleaning product brands, which were up 28%. The growth of maintenance products in Asia Pacific was driven in large by higher sales of WD-40 Multi-Use Product and WD-40 Specialist in China.

In China, sales and maintenance products were up 29%, primarily due to successful brand building programs and the timing of customer orders. On a constant currency basis, sales for China would have increased by 35%. We've consistently shown how effective brand building drives success in markets worldwide. Over the last few years, we've continued to invest slightly higher levels of A&P in brand building activities in priority markets like China. If we push our A&P investment from 5% to 6%, and 8% to 10% in disciplined brand building and sampling programs in such high-growth target markets, we experienced higher levels of growth and returns like we are experiencing in China.

We're regularly focused on building brand awareness through targeted sampling programs or what we refer to internally as putting cans in hands and expanding our distribution network. A simple yet effective strategy that has worked for decades. As a result, we've continued to see strong growth in returns.

In our Asia Pacific distributor markets, sales were up 7%, primarily due to successful brand building programs in certain regions and the timing of customer orders. The growth was driven by higher sales of WD-40 Multi-Use Products, which were up 5% and higher sales of WD-40 Specialist, which were up 33%.

In Australia, we experienced a very strong quarter with solid sales of both WD-40 Multi-Use Product and WD-40 Specialist, which increased 6% and 14%, respectively. Recently volumes have been unfavorably impacted by price increases we had implemented in Australia, which resulted in temporarily reduced demand. The combination of recovering volumes and successful brand building programs have resulted in a strong quarter. In addition, home care and cleaning product sales increased by 28% in Australia.

Our no vac carpet cleaning product portfolio, boost a robust brand presence, a solid competitive edge and significant growth opportunities. In addition, our home care and cleaning brands provide our Australian subsidiary economies of scale. On a constant currency basis, sales for Australia would have increased by 14%. In total, our Asia Pacific segment made up 13% of our global business in the third quarter.

Now let me discuss the progress we've made against our Must-Win Battles and provide you with an update on the strategic enablers that support our Four-by-Four Strategic Framework. Our Must-Win Battles focus on what we do to increase sales and profitability. We look at these Must-Win Battles as long-term growth drivers, and therefore, we'll focus our discussion on the year-to-date results of these battles.

Starting with Must-Win Battle #1, lead geographic expansion. Year-to-date, global sales of WD-40 Multi-Use Product were $334 million, representing growth of 11% over the prior year. We experienced strong sales of our signature Multi-Use Product brand in all 3 trade blocks with 18% growth in EIMEA, 7% growth in the Americas and 5% growth in Asia Pacific. We've made excellent progress in many key markets with strong sales growth of 32% in Latin America, 29% in Benelux, 28% in Iberia, 27% in France, 23% in the Middle East, 22% in Italy, 14% in our DACH region and 9% in China.

The strong growth in Latin America is partially attributable to the acquisition of our Brazilian marketing distributor, which was a strategic decision that aligns with this Must-Win Battle. Much of our initial growth we've seen this quarter is due to the departure from our prior agreement with Theron Marketing, which

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was based on a royalty model. Moving to a direct market provided us with an immediate benefit to our top line, which we're realizing this quarter.

For the first 12 months of direct operation, we expect the Brazil market to contribute revenue growth of more than $10 million due to this transition. This is a substantial increase over the growth expected under the old royalty-based business model. Over the medium term, which is approximately 3 to 5 years, we expect to turn Brazil into a $20 million-plus market.

Sales growth in Latin America is also attributable to increased sales in Mexico. Year-to-date sales of WD-40 Multi-Use Product in Mexico increased 25% over the prior year. As you may recall, we successfully shifted from a distributor model to a direct market in Mexico in May 2020, and our revenues in Mexico have tripled since making that shift and are expected to have virtually quadruple by the end of this fiscal year.

Very similar to our investment strategy in China, we've consistently invested in brand building and expanding our distribution network in Mexico, and our investments are paying off. We're very pleased with our positive starts in our newest direct markets in Brazil and Mexico. We believe this latest acquisition of the Brazil market was a game-changing opportunity for us. We will continue to assess additional markets to uncover further game-changing opportunities ahead.

Next is Must-Win Battle #2, accelerating premiumization. Year-to-date, global sales of WD-40 Smart Straw and EZ-REACH when combined, were $175 million, up $21 million or 14% over the prior year. For us, premiumization is a major contributor to our revenue growth as well as gross margin expansion and our premiumized products are loved by end users around the world. In addition, our premiumized delivery systems are a major driver of growth for our flagship brand and contributed 61% of WD-40 Multi-Use Product growth year-to-date.

Our implementation of WD-40 Smart Straw next generation in the Americas and the multiple packages in EIMEA is contributing to the sales growth of premiumized products. This growth aligns with our long-term net sales compound annual growth rate target of greater than 10% in reported currency for premiumized products.

Our third Must-Win Battle is to drive the WD-40 Specialist growth. Year-to-date, sales of WD-40 Specialist products were nearly $54 million, up 11%. We saw growth of WD-40 Specialist products across all 3 trade blocks with particularly strong growth in EIMEA and Asia Pacific where sales grew 15% each. In China, we experienced spectacular growth in WD-40 Specialist of 47% due to expanding distribution new WD-40 Specialist product introduction to the region as well as successful brand-building programs. We continue to target a net sales compound annual growth rate of greater than 15% in reported currency for WD-40 Specialist.

Our fourth and final Must-Win Battle is to accelerate digital commerce. We see this as an accelerator for all our other Must-Win Battles as it improves brand awareness and online engagement, leading to an improved customer experience and sales across all our trade channels. Some of our key objectives within this Must-Win Battle are to build our brand digitally, grow and develop the e-commerce pure-play channel, accelerate growth of the omnichannel and continued capability building for our employees. Year-to-date, e-commerce sales were up 18%, with double-digit growth across all 3 trade blocks.

Turning to the second element of our Four-by-Four Strategic Framework, our strategic enablers. Our strategic enablers focus on operational excellence and support how we will achieve our Must-Win Battles. Strategic enabler #1 is about ensuring a people-first mindset that call to begin at the very top of our organization with our Board of Directors.

Last month, we shared that Greg Sandfort will retire from our Board as of our next Annual Meeting of Stockholders in December. Our Board intends to nominate Eric Etchart as Nonexecutive Chair following Greg's departure. I'm very pleased that the Board intends to appoint Eric to this role. His breadth of international finance, marketing, board and management experience will provide the company valuable insights as we seek to accelerate our geographic expansion and remain steadfast in our commitment

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to good corporate governance. Eric also has strong appreciation for our culture here and leadership experience in ESG.

Which brings us the strategic enabler #2, build a sustainable business for the future. We will have a very robust update for you on this enabler at our next earnings call because we intend to post our next ESG Report in early fiscal year 2025. And our reports will be articulating our progress on key ESG matters. In addition, we continue to make great progress in our global repair and replace campaign.

In 2021, WD-40 Company launched the repair challenge, an online content that inspires millions of doers, makers, fixes and builders across more than 40 countries to show how they extend the lifespan of their tools, worn down equipment, bicycles, cars or just about anything else to keep them in circulation for longer. To date, the Repair Challenge has created over 0.5 billion marketing impressions with end users worldwide.

Strategic enabler #3 is achieving operational excellence in supply chain. This strategic enabler is meant to continue our quest for operational excellence. To support the strategic enabler we've established a set of global supply chain KPIs that are being utilized by all 3 trade blocks. This allows us to understand our operational performance at a deeper level in all regions. One important KPI is in achieving on time and in-full delivery and I'm happy to share with you big customer OTIF scores are more than 95% in aggregate in the third quarter.

We've also been working on several key projects this year that support the strategic enabler. Since we outsource our manufacturing, it's crucial for us to take responsibility and leadership and ensuring that our entire value chain from raw materials to customers and end users meets the highest standards we set for ourselves and our partner organizations. We are committed to ensuring that our products are manufactured and delivered in accordance with the highest ethical and professional standards.

Good governance is the first step towards good social and environmental responsibility in the supply chain. Therefore, we've recently published a revised supplier code of conduct and are currently working to develop and roll out a new responsible sourcing policy so we can more clearly communicate how the supply chain can positively contribute towards the areas of environmental and social responsibility.

And finally, strategic enabler #4 is to drive productivity by enhanced systems, which Sara will provide you an update on. With that, I'll now turn the call over to Sara.

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

Thanks, Steve. I have several updates for you today, including some additional thoughts around the sale of the home care and cleaning business. But before I begin, I would like to provide an update on our ERP implementation, which has been a significant investment under our strategic enabler #4, which is to drive productivity via enhanced systems.

In the second quarter, we went live with the first phase of our ERP system, which is now in place over a substantial portion of our business, including the U.S., Latin America and Asia regional distributor businesses. Each month that goes by, we experience fewer and fewer issues. And although we did experience some minor disruptions in the third quarter, I am pleased to share that most of the critical issues have subsided by the end of the quarter.

We are currently phasing some of our functional teams out of hyper care which is an indication of the stability of the system. This is a very positive sign and a significant milestone for our ERP team. We know there is still work to do and have several enhancements that are already being worked on, which is not unexpected at this phase of the project. Most importantly, we have gained numerous learning moments from this implementation, allowing us to make process improvements and become more proactive. I want to acknowledge and thank our employees for their ongoing diligence and managing through this implementation.

Our strategic enabler #4 is much more than an ERP system. We are making foundational investments in systems and data that will allow us to grow faster. For example, we have rolled out Salesforce in the

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U.S., and we'll be expanding that further in the near term, driving sales efficiencies and effectiveness and helping us reduce operating costs. We also know that use of data analytics and automated tools leveraging data is increasing and can be a real enabler for the business. The foundational work we are doing now around data governance, centralizing our data architecture and data quality management will allow our people to leverage our data quicker and drive better decision-making. We are making progress on the sale of our U.S. and U.K. home care and cleaning product brands. As a reminder, this business represents only approximately 4% of our total sales.

Post divestiture, WD-40 Company will be a more focused company with a higher sales growth and gross margin profile. We have engaged an investment bank, and they are currently in discussions with potential suitors on our behalf. While there are no certainties on identifying a buyer when going to the market, our expectation is that we will likely complete the divestiture of these brands during fiscal year 2025. We will provide further updates on the divestiture process as appropriate.

And now for an update on our business model. Our asset-light and dynamic business model has helped the company maintain a healthy financial position and generate strong returns for our stockholders for many years, and it continues to be our guiding light. Our 55/30/25 business model is a long-term beacon that we will move toward and align with over time. In the short to mid term, we think about each critical component of the model in a range.

Let's start with our third quarter gross margin performance. We target a range of 50% to 55% for gross margin. and we have made significant progress to perform well within this range. In the third quarter, our gross margin was 53.1% compared to 50.6% last year. This represents an improvement of 250 basis points, which was driven by a few factors. Gross margin benefited 160 basis points from favorable sales mix and other miscellaneous mix. Lower costs associated with specialty chemicals also positively impacted gross margin by 110 basis points. We are pleased to see that for now, the inflationary environment has stabilized. Gross margin was also positively impacted by 70 basis points from lower warehousing, distribution and freight costs, primarily in the Americas segment. We have continued to reduce our inventory levels in the U.S. which is having a positive impact to our gross margin. Gross margin improved over prior year across all trade blocks.

Within the Americas, gross margin improved 240 basis points over prior year to 50.6%. EIMEA continues to expand gross margin, improving 280 basis points over prior year to 54.8%. And Asia Pacific, again, turned in a strong gross margin performance, improving 130 basis points over the prior year to 57.6%. I am very pleased with how gross margin has held up through the duration of fiscal year 2024. And at this point, with less than one quarter to go, we do believe we will come in closer to the high end of the guidance range for gross margin.

Based on the current trajectory, cost environment and macro environment, we are targeting to achieve gross margin of 55% by the end of fiscal year 2026.

Now turning to our cost of doing business, which we define as total operating expenses plus adjustments for certain noncash expenses and is primarily comprised of investments in our employees, investments in our brand and freight expense. As we continue to grow our top line, we also remain focused on operating efficiently and is sustaining the WD-40 Company economy. As we get more operational leverage, we expect the cost of doing business to perform within our targeted range of 30% to 35% over time.

For the third quarter, our cost of doing business was 34% as compared to 32% in the prior year. The increase was primarily driven by increases in employee-related costs due to higher accrued incentive compensation, annual compensation increases and higher head count. We also experienced increase in professional services, including costs associated with our ERP implementation and the acquisition of our Brazilian distributor.

Investments in advertising and promotional activities, or A&P, increased over the prior year quarter as we continue to invest in brand building activities and make investments that support long-term profitable growth. As a percentage of sales, A&P investment was 6% compared to 5.4% in the prior year. Our A&P investments are always impacted by phasing between quarters and we still expect the full year to be within our guidance of 5% to 6%.

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Turning now to adjusted EBITDA margin. While adjusted EBITDA margin has been under pressure due to the inflationary environment and the strategic investments we are making, we continue to target an EBITDA margin range of between 20% and 25% over the longer term. For the third quarter, adjusted EBITDA margin was 19%, which was relatively constant compared to the prior year.

Now let's discuss net income and EPS. Net income of $19.8 million improved approximately $1 million or 5% from prior year. On a constant currency basis, net income would have increased 4% compared to the prior year. Our net income reflects a provision of income tax rate of 23.2%. Diluted earnings per common share for the quarter were $1.46 compared to $1.38 in the prior year. Diluted EPS reflects 13.6 million weighted average shares outstanding this quarter, which was essentially flat compared to the prior year.

Now we'll discuss the word about our balance sheet and capital allocation strategy. The company's financial condition and liquidity remains strong. And our capital allocation strategy includes a comprehensive approach to balanced investing and long-term growth while providing strong returns to our stockholders.

We continue to return capital to our stockholders through regular dividends and buybacks. Annual dividends will continue to be our priority and are targeted at greater than 50% of earnings. On June 18, our Board of Directors approved a quarterly cash dividend of $0.88 per share. During the third quarter, we repurchased 11,250 shares of our stock under our current share repurchase plan at a total cost of approximately $2.8 million. We will continue to be active in the market and expect to repurchase at least enough shares to offset shares issued for equity compensation.

We continue to make progress in lowering our inventory levels, which we had invested in to stabilize our supply chain in prior years. Our inventory levels peaked in the first quarter of fiscal year 2023. And since then, we have reduced inventory by nearly $43 million or 36%. Our cash flow from operations year-to-date for fiscal year 2024 was approximately $65 million, and we elected to use approximately $12 million of that cash to pay down a portion of our short-term higher interest rate borrowings. Our intent is to continue to pay down higher interest rate borrowings under the current interest rate environment in the near term. That concludes my discussion on our reported results.

Let me now provide an update on our guidance. We are pleased that the business is performing in line with our expectations. We continue to believe our current guidance is our best estimate. And for that reason, we are reiterating our outlook for fiscal year 2024 today.

Net sales growth is projected to be between 6% and 12% with net sales between $570 million and $600 million in constant currency. Gross margin is expected to be between 51.5% to 53%. However, as I mentioned earlier, we do believe we will come in closer to the high end of the guidance range. Advertising and promotion investment is projected to be between 5% and 6% of net sales. The provision for income tax is expected to be between 23% and 24%. Net income is expected to be between $67.7 million and $71.8 million and diluted earnings per share is expected to be between $5 and $5.30, which is based on an estimated 13.6 million weighted average shares outstanding. Also, as a reminder, this guidance assumes no major changes to the current economic environment. Unanticipated inflationary headwinds and other unforeseen events may affect our view of fiscal year 2024. That completes the financial overview.

Now I would like to turn the call back to Steve.

Steven A. Brass
CEO, President & Director

Thank you Sara, for that update. I'm pleased with both the top line and the bottom line results we've experienced this quarter. While I'm always happy to see a strong quarter, what's more important is long-term trends. As a reminder, our long-term growth target is to increase maintenance product sales within the Americas by 5% to 8%, within EIMEA by 8% to 11% and within Asia Pacific by 10% to 13%. For full fiscal year 2024, all 3 of our trade blocks are expected to perform at or above these levels.

In summary, what did you hear from us on this call? You heard that for the third quarter, we reported consolidated net sales of $155 million, an increase of over 9% over prior year and a new record for the

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company. You heard the volumes continue to improve. And in the third quarter, nearly all our sales growth was driven by volume.

You heard that sales of maintenance products grew over 10% in both the third quarter and year, which is in line with our long-term growth targets. You heard that we're making good progress on the sale of our U.S. and U.K. home care and cleaning product brands. You heard that we continue to execute in our Must-Win Battles, sales of WD-40 Multi-Use Product and WD-40 Specialist were both up 11% year-to-date. Premiumization sales grew by 14%, and at year-to-date our digital commerce sales grew by 18%.

You heard that our newest direct market in Brazil is off to a strong start and that we believe the acquisition of the Brazil market was a game-changing opportunity for us. You heard that gross margin continues to improve and that we believe will come in closer to the high end of the guidance range for gross margin this fiscal year. You heard that we continue to make progress in lowering our inventory levels and that we have reduced them by nearly 36% since peak levels.

You heard that for the full fiscal year 2024, all 3 of our trade blocks are expected to perform at or [above] our long-term growth targets for maintenance product sales. And you heard that we are reiterating our guidance for fiscal year 2024.
Thank you for joining our call today. We'd now be pleased to answer your questions.

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Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Linda Bolton-Weiser with D.A. Davidson.

Linda Ann Bolton-Weiser
D.A. Davidson & Co., Research Division

Congratulations on a nice quarter. So I was wondering if you could just give us a little bit of color on the gross margin outlook. I guess in the shorter term, would it be fair to say that for FY '25, it would continue on at least at the point at which gross margin ends FY '24? So if you end over 53% gross margin that would carry over at least at that level. Is that the right way to think about it for FY '25?

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

Linda, this is Sara. So yes, we are right now tracking towards the high end of our range for FY '24. We haven't really given -- we don't really give guidance on FY '25 until we get to the end of the year. But I think as we've indicated, we are targeting to get back up to the 55% by the end of FY '26. And so obviously, we have to make some of that up in FY '24, and we have a number of initiatives that we're working towards to help move the needle from where we believe we will end the year, which is going to be at the high end of the range to the $55 million at the end of FY '26.

Linda Ann Bolton-Weiser
D.A. Davidson & Co., Research Division

So I'm just curious on that slightly longer-term target. What gives you confidence that you can project that because you do have a lot of moving pieces that affect your gross margin, in particular, the input costs. Is it just that you have so many things in the pipeline of different initiatives you can do. Can you give us a flavor for just a couple -- touch on maybe a few of those things that give you confidence.

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

Sure. So when we look at the road map to getting back up to the 55%, it's really breaks down into about 3 buckets. The first one is what we've talked about in the past around premiumization and sales mix. So selling more in our -- growing faster in our markets where we are -- where we earn a higher margin as part of that and also expanding on our premiumization. So selling more Smart Straw, easy region specialists in many regions. So that's the first bucket.

The second bucket is really driven by operational efficiency in the supply chain. So there are a number of smaller projects that we have in the pipeline that we believe are going to help decrease our costs over time, and that will take -- those projects to expand over the next couple of years.

And then the third is there still will be some movement on price. So we haven't moved on price this year, and we don't really have any immediate intentions to move on price in the near term. but there will be some pockets. We believe as we get out into the later half of FY '25, maybe and into FY '26 of just more targeted tactical price increases at a much smaller scale, but that will also help us get back up to the 55%. You are correct, input costs can fluctuate and we don't necessarily have control over those. But we believe based on the current cost environment that the initiatives we have in place will get us back to the 55%.

Linda Ann Bolton-Weiser
D.A. Davidson & Co., Research Division

Okay. And then I was just wondering about -- I mean, it sort of looks from the numbers that your prior year comparison on sales growth was much harder in the third quarter and easier in the fourth quarter. But I think that has to do with some of the cadence having to do with the impacts from stuff in China or the pandemic or something. So like maybe you can just give us some color on like is that fourth quarter

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prior year comp really easier? Or is it just normal? And how do you feel about like where along that range for the sales for the year? Like are you most comfortable toward the lower end, middle, higher end? Is there any color you can give.

Steven A. Brass
CEO, President & Director

So in terms of the third kind of phasing by quarter, so what you're seeing this year, Linda, that's kind of been kind of abnormal recovery, right, has been the volume recovery in Europe and in Latin America. So we talked about it at the start of the year. So where you saw that really strong volume recovery in the Americas, certainly in the U.S. last year, you've seen that continue through. There is a specific dynamic in Q4 with Asia Pacific, which had a very weak quarter last year.

So I think the number last year in Asia Pacific is 15 million or something. And so we have a very soft comparable number for Q4 in Asia Pacific. But I think the reason you're seeing such big continued strong growth what was driving the entire company has been Latin America come back, if you like. And then EIMEA very, very strong volume recovery, especially in those direct markets we highlighted.

Linda Ann Bolton-Weiser
D.A. Davidson & Co., Research Division

Okay. So then just following up on what you said about the Asia Pacific comparison, I mean, if it is indeed easy in the fourth quarter then growth should be sort of strong in the fourth quarter of '24. Is that the way to think about it?

Steven A. Brass
CEO, President & Director

Also we guided towards Asia Pacific being within the traditional range of growth between 10% and 13%, and it's not there today. So yes, we're expecting a strong Q4 in Asia Pacific.

Linda Ann Bolton-Weiser
D.A. Davidson & Co., Research Division

Okay. And then again, I know you don't want to get too much into the next fiscal, of course, but I'm just wondering if you could -- if there's any quantification of maybe some unusual costs that were related to ERP implementation or some other projects that might dissipate in the next fiscal year that would create a favorable comparison. Is there anything like that, that you're kind of aware of in a general sense?

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

I mean, we have been spending higher this year as a result of the timing of the go-live for the ERP. So if we look at our general IT investments for this year, they are going to be trending higher than they -- than they have compared to the prior years. We are in the current budget cycle right now. So we're working on taking a look at where are we going to land next year from an IT investment standpoint and other investments. But that's probably the biggest area that when you look at the past few years, that has trended up as a result of us getting closer to our go-live date. We are continuing to invest in IT, though. I mean we do have that Wave 2 coming around, but we don't believe the cost of the Wave 2 is going to be at the same level as this current -- the current wave that we just pushed out earlier in the year.

Operator

Our next question comes from the line of Daniel Rizzo with Jefferies.

Daniel Rizzo
Jefferies LLC, Research Division

I may have missed this, but you mentioned the ERP rollout in the Americas and Asia. I am sorry, did it already occur in Europe? Or is that something that's going to be -- you're going to be doing over the next several quarters?

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Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

So it did not incur and this did not happen in Europe. So we went live impacting our U.S. business, our Latin America business and our Asia regional distributors, which represents about 50% of our revenues. So we still have about 50% of our revenues. The majority of that is in Europe. That's on another system. And then we have 2 other really small systems for a couple of our other international locations.

Daniel Rizzo
Jefferies LLC, Research Division

So you're going to be merging the European system with this system. Is that -- I mean, ultimately, is that the goal?

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

So our Wave 2 right now is targeted towards 2 of our smaller locations that are still on the old system that we just came off of. So our first priority is to get off of that old system. These other 2 locations are individually less than 5% of our revenues. So they're much smaller implementations. And then we are working on obviously bringing Brazil in through the acquisition. So that's a priority for us. And then we are looking at our road map beyond those -- that next phase. But that next phase is our immediate priority. And then we are, Daniel, looking at -- what -- is it appropriate for us to bring everybody else on to the one system?

Daniel Rizzo
Jefferies LLC, Research Division

Okay. And then just kind of following up on the questions that were just asked. With -- I mean, you can get to 55% if things stay the same. Is there a certain band that oil, tinplate and plastic has sustained for you to hit that? I mean if there's a spike, then that kind of changes the dynamics, correct? Particularly the [indiscernible].

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

I would say if there's a spike and it's temporary, right? That's what we just drive that wave. If there is a spike of, let's say, $20 to $25 to $30 and it stays there for an extended period of time, that's when we would have to take a look and see if we want to do -- if there are other levers that we would want to pull to try to offset that. But usually, if it fluctuates within $20 directionally one way or the other, and we tend to ride that wave over time.

Daniel Rizzo
Jefferies LLC, Research Division

Okay. And then -- and my final question is just kind of for maintenance. If I look at like unallocated expenses, I think it's been a little bit higher than what had been previously and maybe higher than what I was modeling. I was wondering if what you're doing now is kind of the run rate going forward for the next couple of years, which is roughly, I don't know, call it, I think -- what -- $48 million?

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

Yes. The unallocated expenses. So one of the biggest drivers of that, that's ticked up is associated with the ERP. So we funded that out of the corporate expenses. And so that's sitting in the unallocated corporate. So that's probably been the biggest driver, Daniel, that you'll see there from a trend perspective.

Daniel Rizzo
Jefferies LLC, Research Division

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And that's going to be rolling off. I mean, as we focus now on smaller systems around Brazil, that's going to be that same it would be less then, correct?

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

So I think our trajectory is not going to be at the same trajectory that it was this year, but it will not drop down to nothing. I mean we will still be investing as we have to roll out those other waves.

Operator

Our next question comes from the line of Rosemarie Morbelli with Gabelli fund.

Rosemarie Morbelli

Following up on Linda and actually Dan's question regarding IT spending, are you sharing the amount you have spent towards that new ERP system. What was your IT spending in 2023? What is it in 2024? And what are we looking at for '25 and '26, if you can share those numbers?

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

We have not disclosed the individual year that we've -- within the individual years, how much we have been spending on IT. We did disclose that the total cost of what we went live and what we placed in what we went live with in Q2 was approximately $10 million, and we will be amortizing that over 10 years. And so we did disclose the total cost of that first wave that was sitting on the balance sheet. But there were other costs that did not qualify for capitalization. And we really incurred those costs over roughly about 4, maybe 4.5 years to give some perspective.

Rosemarie Morbelli

So if we look at -- if we don't look at IT spending specifically, but look at your CapEx level. So is it in CapEx? And what were -- what do you expect the CapEx to be this year and then next year?

Sara Hyzer
VP of Finance, Treasurer, CFO & Principal Accounting Officer

So there is a nuance about the cloud-based costs that were capitalized. Those are actually not in CapEx. So those costs are sitting on our balance sheet and other long-term assets and do not show up in our investing cash flow line items. And so there's accounting rules that require us to present the cost that we capitalize for the new system because it's cloud-based differently than normal capital expenditures. So our normal capital expenditure, where we are right now in maintenance mode. We expect that to be between our normal 1% to 2% of our revenue levels, and that's what we're trending at this year.

So the place to really look on our balance sheet to look at the capital -- to look at the ERP costs specifically is the increase in our long-term asset over time.

Rosemarie Morbelli

Okay. And then if I may, you are showing good growth on the -- for the specialties category, which obviously is one of your Must-Win category. Within that category, are there specific product, product lines, applications that are growing faster than others. And by the same token, there are some which you don't think are going to do very well and you might consider eliminating them from the bucket of specialist products?

Steven A. Brass
CEO, President & Director

Thank you, Rosemarie. So I mean, yes, we have around 6 SKUs, 6 products around the world. They're pretty consistent. We haven't disclosed what those products are. But those products account for around 80% of WD-40 Specialist sales. And so as a global learning organization, we share -- we have teams that

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get together and share best practice approaches to building those brands across the world. And so very much focused on those core products within the specialist range. And that's what's driving expanding distribution and then putting samples in the right people's hands around the world is what's driving the growth, the double-digit growth WD-40 Specialist. And then on the other side, yes, products were not perfect, and so if products come out that don't perform, they get called and replaced with more promising options.

Rosemarie Morbelli

Okay. Eventually, you will give us a better feel for the different categories?

Steven A. Brass
CEO, President & Director

So I mean if you look at the longest kind of running products in our portfolio, then that's because they've been around the longest, we started most places, the likes of silicones, penetrants, [indiscernible] greases, et cetera. That's kind of where we started with WD-40 Specialist and they're some of the key sellers.

Operator
Ladies and gentlemen, that does conclude our allotted time for questions. We thank you for your participation on today's conference call and ask that you please disconnect your lines.

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