Williams-Sonoma (WSM)

Updated August 23rd, 2018 by Jonathan Weber

Key Metrics

Current Price:	$63	**5 Year CAGR Estimate:**	9.3%	**Volatility Percentile:**	83.1%
Fair Value Price:	$67	**5 Year Growth Estimate:**	5.3%	**Momentum Percentile:**	91.3%
% Fair Value:	94%	**5 Year Valuation Multiple Estimate:**	1.2%	**Valuation Percentile:**	46.8%
Dividend Yield:	2.8%	**5 Year Price Target**	$86	**Total Return Percentile:**	39.0%

Overview & Current Events

Williams-Sonoma is a specialty retailer that operates home furnishing and houseware brands such as Williams-Sonoma, Pottery Barn, West Elm, Rejuvenation, Mark & Graham and others. Williams-Sonoma operates traditional brick-and-mortar retail locations but sells its goods through e-commerce and direct-mail catalogs as well. Williams-Sonoma was founded in 1956, is headquartered in San Francisco, and is currently valued at $5.2 billion.

Williams-Sonoma reported its most recent quarterly results on August 22. The company earned $0.77 per share during Q2. Revenues totaled $1.3 billion during the second quarter, an increase of 7% compared to the prior year's quarter. This was primarily due to a strong comparable sales growth rate of 4.6%. Williams-Sonoma has raised its guidance for 2018. The company now sees revenues of $5.6 billion, and earnings per share are forecasted at $4.31 (at the midpoint).

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$0.28	$0.72	$1.83	$2.22	$2.54	$2.82	$3.24	$3.37	$3.41	$3.61	***$4.31***	***$5.58***
DPS	$0.48	$0.48	$0.55	$0.73	$0.88	$1.24	$1.32	$1.40	$1.48	$1.56	***$1.72***	***$2.36***
Shares	106M	107M	105M	100M	98M	94M	92M	90M	87M	84M	***80M***	***68M***

Williams-Sonoma has a solid growth history. Over the last five years its EPS grew by seven percent annually. Its growth since 2008 has been a lot stronger, but 2008 had been a very weak year due to the impact of the last financial crisis. Unlike many other retailers Williams-Sonoma has been able to increase its profits through the last couple of years, which is, among other factors, due to its consistent revenue growth. Thanks to its omni-channel sale strategy Williams-Sonoma has established a strong e-commerce business. The majority (53% during Q2) of the company's sales are already derived from its online retail platforms. Online sales rose by another 9% in the second quarter.

Guidance for FY 2018, which sees EPS growing by 19% year over year, is impacted by two special items that will lead to unusually high growth. The first one is the impact of a 53rd week in fiscal year 2018 (versus 52 weeks in FY 2017). The other is the impact of tax law changes, which will significantly lower Williams-Sonoma's tax rate going forward.

Williams-Sonoma unfortunately was not able to keep its margins flat, or expand them further, during the last year. The company's operating margin declined from 9.6% to 8.9%. This lowers Williams-Sonoma's organic earnings growth, as revenue growth and margin depression roughly offset each other. Williams-Sonoma forecasts another small margin decline for 2018. Earnings per share growth, when adjusted for tax rates, has been primarily driven by share repurchases in 2017. Those share repurchases will be a key factor for EPS increases going forward, too, as Williams-Sonoma has announced a new $500 million buyback program that could lower its share count by ~10%.

Williams-Sonoma's dividend grew 7% annually over the last five years, in line with its earnings-per-share growth.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	---	21.6	15.8	16.6	15.8	19.4	20.8	22.2	15.5	14.1	***14.6***	***15.5***
Avg. Yld.	2.7%	3.1%	1.9%	2.0%	2.2%	2.3%	2.0%	1.9%	2.8%	3.1%	***2.8%***	***2.7%***

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

Williams-Sonoma's valuation has declined considerably over the last couple of years. Shares are not as inexpensive as they were earlier this year, when Williams-Sonoma's share price was in the $40s. Right now shares look slightly undervalued, which should result in a small tailwind from multiple expansion over the coming years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	73.7%	58.8%	52.9%	64.3%	70.9%	72.6%	72.6%	77.3%	76.0%	75.6%	***75.0%***	***73.0%***
Debt/A	44.5%	40.7%	41.8%	40.8%	39.3%	40.2%	46.2%	47.6%	50.4%	49.6%	***50.0%***	***50.0%***
Int. Cov.	---	220	105	910	---	---	---	---	780	690	***650***	***500***
Payout	171%	66.7%	30.1%	32.9%	34.6%	44.0%	40.7%	41.5%	43.4%	43.2%	***39.9%***	***42.3%***
Std. Dev.	63.3%	55.2%	37.5%	37.7%	26.8%	20.8%	26.1%	21.9%	29.5%	25.3%	***29.0%***	***28.0%***

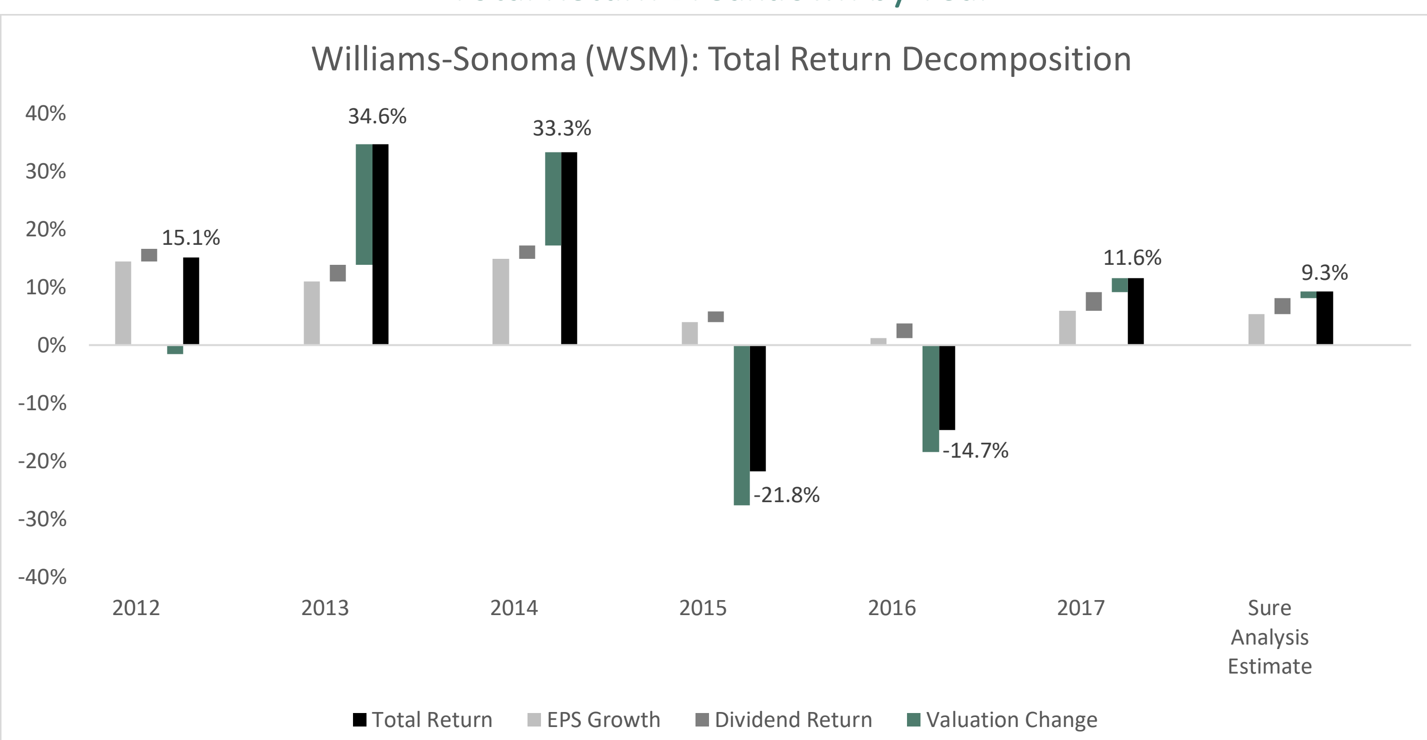
Williams-Sonoma operates a relatively asset-light business model relative to other retailers, thanks to a high portion of sales that are not made at brick-and-mortar stores. Combined with high asset turnover this allows for very high gross profits relative to the assets it owns. Roughly half of the company's assets are financed via liabilities, but the majority of those liabilities are not interest-bearing long term debt, but rather items such as accounts payable and customer deposits. Due to a low portion of interest-bearing liabilities Williams-Sonoma's interest expenses are very low.

Williams-Sonoma competes with different companies. Traditional brick-and-mortar home improvement retailers such as Home Depot and Lowe's, which are both significantly larger, but also with e-commerce players such as Amazon. Williams-Sonoma's product portfolio is relatively unique, though, as the combination of the products it sells is not offered by competitors. Williams-Sonoma's business model is relatively cyclical, as consumers tend to avoid purchases of discretionary during economic downturns. Williams-Sonoma suffered an earnings decline of 60% from 2007 to 2009.

Final Thoughts & Recommendation

Williams-Sonoma is a small, ecommerce-focused retailer that has established a profitable niche. Margin pressures are a headwind, but comps sales look promising. Going forward shareholder returns via dividends and buybacks will play a major role for Williams-Sonoma's total returns. Shares have risen by 30% over the last couple of months and look relatively fairly valued right now, which is why we rate them a hold for now.

Total Return Breakdown by Year



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