



H.B. Fuller (FUL)

Updated January 17th, 2019 by Aristofanis Papadatos

Key Metrics

Current Price:	\$39	5 Year CAGR Estimate:	11.5%	Volatility Percentile:	53.8%
Fair Value Price:	\$49	5 Year Growth Estimate:	5.0%	Momentum Percentile:	30.6%
% Fair Value:	79%	5 Year Valuation Multiple Estimate:	4.9%	Growth Percentile:	31.7%
Dividend Yield:	1.6%	5 Year Price Target	\$63	Valuation Percentile:	59.8%
Dividend Risk Score:	A	Retirement Suitability Score:	B	Total Return Percentile:	35.6%

Overview & Current Events

H.B. Fuller is a leading global formulator, manufacturer and marketer of adhesives, sealants and other specialty chemical products. The category of industrial adhesives is the core product offering of the company.

Given the \$2.0 billion market cap of H.B Fuller, it is evident that its acquisition of Royal Adhesives & Sealants for \$1.6 billion is critically important. This acquisition, which is the largest in the history of the company, boosted its annual sales by \$735 million (32% growth) and enhanced its reach to more highly specialized adhesive segments. H.B. Fuller also acquired Adecos in late 2017 to improve its growth prospects in Brazil. Thanks to these acquisitions, H.B. Fuller expects to double its EBITDA, from about \$300 million in 2017 to \$600 million in 2020.

In mid-January, H.B. Fuller reported (1/16/19) its financial results for the fourth quarter of fiscal 2018. In the quarter, the company grew its organic sales by 4% thanks to price hikes and double-digit growth in engineering adhesives, which generate about 1/6 of total revenues and 1/5 of earnings. The company enhanced its gross margin from 26.6% to 28.1% thanks to price hikes and synergies from its acquisitions. However, unfavorable currency rates and slower growth in China led the company to miss analysts' earnings-per-share estimates by a wide margin (\$0.90 vs. \$0.99). As a result, the stock plunged 10% in after-hours trading.

Management provided positive guidance for this year. Assuming that macro challenges in China and the strong dollar will persist, management expects 3%-5% organic revenue growth and adjusted earnings-per-share of \$3.15-\$3.45. The mid-point of the guidance implies 10% earnings-per-share growth over last year.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$1.70	\$1.43	\$1.79	\$1.90	\$1.89	\$0.97	\$1.69	\$2.42	\$1.13	\$3.00	\$3.30	\$4.21
DPS	\$0.27	\$0.28	\$0.30	\$0.33	\$0.39	\$0.46	\$0.51	\$0.55	\$0.59	\$0.62	\$0.64	\$0.84
Shares	48.7	49.2	49.5	49.8	50.2	50.3	50.1	50.1	50.2	52.0	52.5	55.0

H.B. Fuller has missed analysts' earnings-per-share estimates in 5 out of the last 7 quarters. This is a reminder that there is a high degree of uncertainty in this business and investors should maintain conservative expectations in order to avoid negative surprises. While the company has grown its earnings-per-share at a 6.5% average annual rate in the last nine years, its record has been markedly volatile. Moreover, H.B. Fuller is highly vulnerable to recessions and a recession has not shown up for nine consecutive years. Therefore, it is prudent to be somewhat conservative and assume 5.0% annual earnings-per-share growth for the next five years.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	10.2	14.9	12.0	15.7	21.5	48.1	24.1	17.7	46.9	17.1	11.8	15.0
Avg. Yld.	1.6%	1.3%	1.4%	1.1%	1.0%	1.0%	1.3%	1.3%	1.1%	1.2%	1.6%	1.3%

Since our last research report, in which we recommending avoiding the stock, H.B Fuller has plunged 26%. As a result, it is now trading at a price-to-earnings ratio of 11.8, which is much lower than its historical average of 16.7. Due to the

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challenges facing the business and its high cyclicality, we assume a fair price-to-earnings ratio of 15.0 for this stock. If the stock approaches our fair valuation level over the next five years, it will enjoy a 4.9% annualized gain thanks to the expansion of its earnings multiple.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	15.9%	19.6%	16.8%	17.4%	20.6%	47.4%	30.2%	22.7%	52.2%	20.7%	19.4%	20.0%

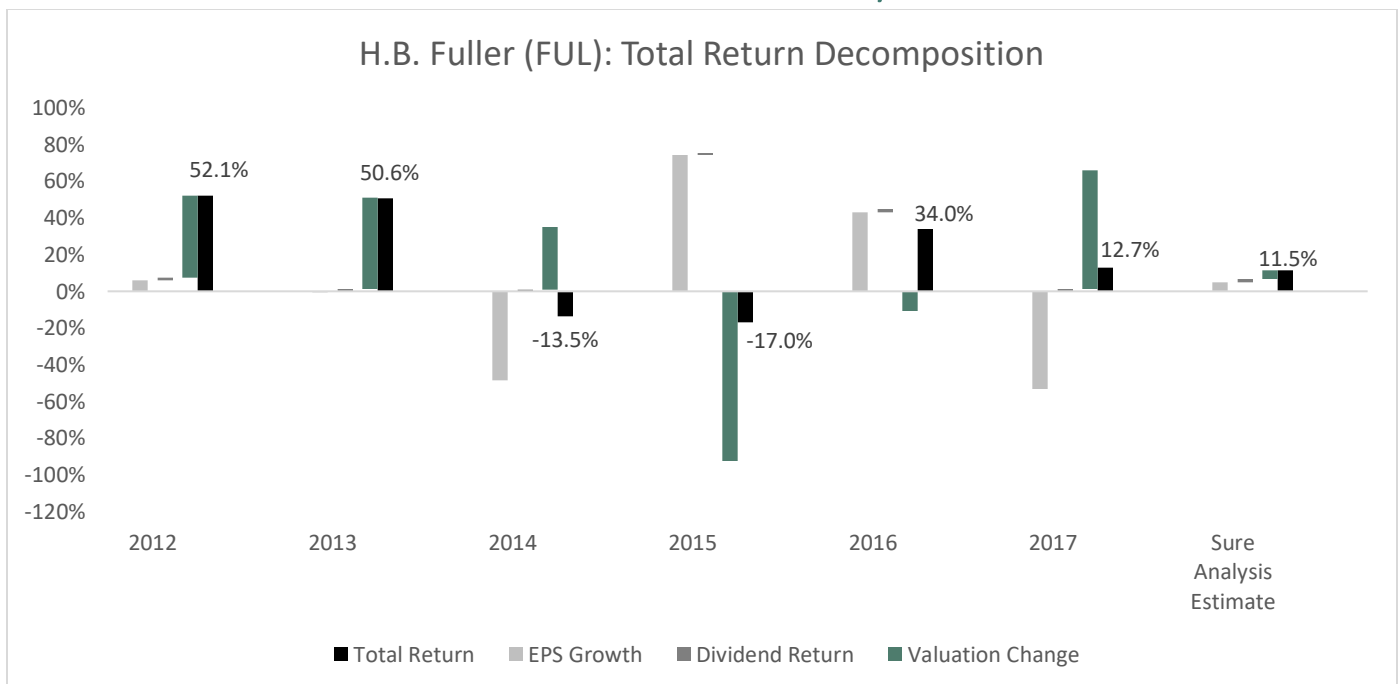
Due to the recent major acquisition, interest coverage has plunged to an almost decade low of 2.6. However, management has repeatedly confirmed that it will be using a major portion of free cash flows to reduce debt. The company reduced its debt by \$204 million last year and expects to reduce it by another \$200 million this year. As a result, its interest coverage is likely to revert towards its historical values in the upcoming years.

As the customers of H.B. Fuller are manufacturers of a wide range of products, the performance of H.B. Fuller is closely tied to underlying economic conditions. The company is highly vulnerable to recessions. During the Great Recession, its earnings per share plunged 79%, from \$1.68 in 2007 to \$0.36 in 2008, and the stock lost 2/3 of its market cap in less than six months. As a recession has not occurred for nine consecutive years and interest rates are on the rise, investors should take this risk factor into account, especially given the company's increased leverage.

Final Thoughts & Recommendation

Since our last research report, in which we recommending avoiding the stock, H.B Fuller has plunged 26%. Consequently, the stock has become much more attractive and can now offer an 11.5% average annual return over the next five years. However, investors should note its volatile earnings record, its vulnerability to economic downturns and its somewhat disappointing business performance. Given the low dividend yield and the huge downside risk in the event of a recession, income-oriented investors should avoid the stock. Moreover, we still advise all the investors to wait for a lower entry point unless they have great confidence in the U.S. economic growth over the next few years.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	1392	1235	1257	1444	1886	2047	2104	2084	2095	2306
Gross Profit	364	371	358	404	517	570	533	568	610	603
Gross Margin	26.2%	30.1%	28.5%	28.0%	27.4%	27.9%	25.3%	27.3%	29.1%	26.2%
SG&A Exp.	255	264	264	291	358	350	362	371	379	447
D&A Exp.	46	47	39	39	57	62	70	75	78	87
Operating Profit	110	107	95	113	138	196	150	170	202	126
Operating Margin	7.9%	8.7%	7.5%	7.8%	7.3%	9.6%	7.1%	8.2%	9.7%	5.5%
Net Profit	19	84	71	89	126	97	50	87	124	58
Net Margin	1.4%	6.8%	5.6%	6.2%	6.7%	4.7%	2.4%	4.2%	5.9%	2.5%
Free Cash Flow	23	49	40	55	73	6	-110	152	132	86
Income Tax	-6	37	20	31	30	40	34	56	50	9

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	1081	1100	1153	1228	1786	1873	1869	2042	2056	4361
Cash & Equivalents	80	100	133	155	200	155	78	119	142	194
Accounts Receivable	206	204	221	217	320	331	341	365	351	474
Inventories	143	117	122	116	209	222	251	249	247	360
Goodwill & Int. Ass.	237	245	240	242	488	483	452	567	572	2338
Total Liabilities	543	506	519	518	1008	943	979	1169	1118	3317
Accounts Payable	133	109	102	104	163	202	174	178	163	268
Long-Term Debt	240	214	251	232	520	493	575	723	703	2452
Shareholder's Equity	536	591	632	705	778	930	890	873	938	1044
D/E Ratio	0.45	0.36	0.40	0.33	0.67	0.53	0.65	0.83	0.75	2.35

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	1.5%	7.7%	6.3%	7.5%	8.3%	5.3%	2.7%	4.4%	6.1%	1.8%
Return on Equity	2.8%	14.8%	11.6%	13.3%	16.9%	11.3%	5.5%	9.8%	13.7%	5.9%
ROIC	2.2%	10.5%	8.4%	9.8%	11.2%	7.1%	3.4%	5.7%	7.7%	2.3%
Shares Out.	48.7	49.2	49.5	49.8	50.2	50.3	50.1	50.1	50.2	52.0
Revenue/Share	26.85	25.14	25.34	28.96	37.26	40.03	41.06	40.54	40.85	44.67
FCF/Share	0.45	0.99	0.80	1.11	1.44	0.12	-2.15	2.96	2.58	1.66

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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