NACCO Industries (NC)

Updated March 9th, 2019 by Nate Parsh

Key Metrics

Current Price:	$37	**5 Year CAGR Estimate:**	13.0%	**Volatility Percentile:**	99.6%
Fair Value Price:	$60	**5 Year Growth Estimate:**	1.0%	**Momentum Percentile:**	36.2%
% Fair Value:	62%	**5 Year Valuation Multiple Estimate:**	10.2%	**Growth Percentile:**	2.1%
Dividend Yield:	1.8%	**5 Year Price Target**	$63	**Valuation Percentile:**	98.0%
Dividend Risk Score:	B	**Retirement Suitability Score:**	D	**Total Return Percentile:**	71.4%

Overview & Current Events

NACCO Industries is a holding company for The North American Coal Corporation, which incorporated in 1913. The company supplies coal from surface mines to power generation companies. At 35 million tons of annual production, NACCO Industries is the largest lignite coal producer in the U.S. and ranks among the top ten of all coal producers. NACCO Industries operates in the states of North Dakota, Texas, Mississippi, Louisiana and on the Navajo Nation in New Mexico. The company has a current market capitalization of $256 million and annual revenues of $135 million.

The company has been very active in purchasing and spinning off a wide variety of businesses in recent years. In 1988 and 1990, NACCO Industries made several purchases that expanded the business to include housewares. In 2012, NACCO Industries spun off its Materials Handling Group (a combination of Yale Materials Handling Corporation and the Hyster Company). The company completed its spinoff of its housewares-related business on 9/29/2017.

NACCO Industries announced fourth quarter and full year results on 3/6/2019. The company earned $1.57 for the quarter, a 12% increase from the previous year. Revenues grew 48% to $39 million. For the year, earnings-per-share improved 21% to $5.00. Revenue increased 29% to $135.4 million in 2018. Coal was the primary driver of growth for the company in the fourth quarter. Unconsolidated coal deliveries improved 6% to 9.2 million tons. Consolidated coal shipments were higher by 60%. Unconsolidated coal is easier to acquire because it is found among loose materials where consolidated coal is found among solid rock. Demand for both consolidated and unconsolidated limestone was high during the quarter, with a 13% increase in limestone deliveries. NACCO Industries ended 2018 with $85.3 million in cash against a debt position of $11 million. The company was able to remove $47 million in debt from its balance sheet during the year. The company has ~$23 million, or 9% of its current float, remaining on its buyback authorization.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$1.03	$9.53	$14.86	$5.02	$5.79	$3.98	$3.13	$4.32	$4.14	$5.00	***$5.00***	***$5.26***
DPS	$2.07	$2.09	$2.12	$1.88	$1.00	$1.02	$1.05	$1.07	$0.98	$0.66	***$0.66***	***$1.31***
Shares	8	8	9	8	8	7	7	7	7	6	***6***	***5***

Because NACCO Industries spun off its Materials Handling Group in 2012, it is not appropriate to compare today's company to the pre-spinoff equivalent. NACCO saw its earnings per share decline 6.5% per year through 2017. Management has not offered guidance for 2019, but the company did perform better last year. Although NACCO has shown negative growth since 2012 and volatile earnings-per-share since then, we are increasing our projected growth to 1% from 0%. This is due to recent improvements in both coal and limestone deliveries.

Adjusting for the spin-off of its housewares business, NACCO Industries increased its dividend 92% for last December's payment. While the dividend has grown by 11.6% per year over the past 5-years, the company will likely be unable to match this growth rate unless earnings cease their decline. With a targeted payout ratio of 25%, near the average since the spinoff of the Materials Handling Group, shareholders are likely looking at $1.31 in dividends-per-share by 2024.

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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	Now	2024
Avg. P/E	41.6	8.9	6.2	18.4	10.0	13.8	16.8	14.5	18.2	8.7	***7.4***	***12.0***
Avg. Yld.	4.8%	2.5%	2.3%	2.0%	1.7%	1.9%	2.0%	1.7%	1.3%	1.8%	***1.8%***	***2.1%***

Shares of NACCO Industries are higher by $1 since our November 5th update. Focusing on just the past 5 years, NACCO Industries shares have traded with an average price to earnings multiple of 14.4. This is significantly higher than the stock's current multiple of 7.4. Investors are just not willing to pay for a company that has declining earnings while the rest of the investment world enjoys an extended bull market. NACCO Industries needs to prove it can reliably grow earnings-per-share before it reaches its 5-year historical averages. We are targeting a price-to-earnings ratio of 12.0 for the stock. If achieved, this would add 10.2% in annual returns over the next five years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	201%	22%	14%	38%	17%	26%	34%	25%	24%	13%	***13%***	***25%***

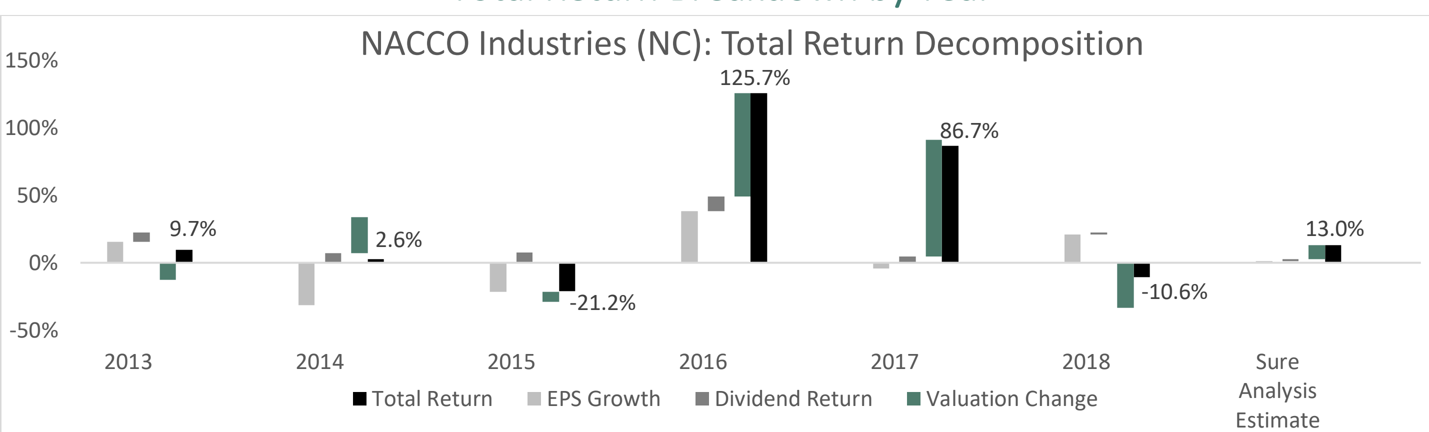
The previous version of NACCO Industries actually saw earnings improve during the last recession, but this is not the same company. NACCO Industries now sees a substantial portion of revenues from coal. As demand for coal fluctuates, so will the company's ability to produce revenue. On the plus side, NACCO Industries has managed to maintain or lower its debt to asset ratio in recent years. The company has also kept its payout ratio low in recent years, which is a prudent decision by management as earnings-per-share continues to drop.

NACCO Industries' primary competitive advantage is that it doesn't acquire existing coal mines or mining companies, as this would increase its leverage position. Instead, NACCO Industries focuses on reducing coal production costs and maximizing efficiency and operating capacity at the mine locations.

Final Thoughts & Recommendation

After fourth quarter results, we expect that NACCO Industries can offer a total annual return of 13%, up from our previous estimate of 8.4%. Much of the gain in expected total return is due to a very low valuation against our 2024 target. Investors willing to deal with fairly volatile earnings-per-share results could be enticed by the potential for double digit total returns from NACCO Industries. We feel, however, that only those investors with a very high tolerance for risk should consider purchasing shares of NACCO Industries due to its poor track record of growth. We have raised our 2024 price target $13 to $63 due to improvements in earnings-per-share, but rate the stock a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	2311	886	790	873	933	897	148	111	105	135
Gross Profit	408	246	210	226	221	185	-11	12	17	30
Gross Margin	17.7%	27.8%	26.5%	25.9%	23.7%	20.6%	-7.6%	10.9%	16.1%	22.1%
Operating Profit	30	94	18	16	18	-17	-54	-39	-33	-22
Operating Margin	1.3%	10.6%	2.2%	1.8%	2.0%	-1.9%	-36.4%	-35.4%	-31.2%	-16.4%
Net Profit	31	80	162	109	44	-38	22	30	30	35
Net Margin	1.3%	9.0%	20.5%	12.4%	4.8%	-4.3%	14.9%	26.7%	29.0%	25.7%
Free Cash Flow	124	47	135	98	-4	-38	104	84	26	34
Income Tax	21	16	33	16	11	-38	-10	-10	1	7

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	1489	1658	1809	776	810	771	655	668	390	377
Cash & Equivalents	256	262	154	140	95	61	52	69	102	85
Accounts Receivable	315	426	97	121	121	123	111	13	15	21
Inventories	337	447	161	169	184	190	165	29	30	31
Goodwill & Int. Ass.	64	60	58	70	60	67	63	46	44	41
Total Liabilities	1092	1210	1232	495	512	559	454	448	170	126
Accounts Payable	272	415	94	127	133	134	100	7	8	8
Long-Term Debt	410	392	148	178	184	248	170	96	58	11
Shareholder's Equity	397	447	576	281	298	211	201	220	219	251
D/E Ratio	1.03	0.88	0.26	0.63	0.62	1.17	0.85	0.44	0.27	0.04

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	2.0%	5.1%	9.3%	8.4%	5.6%	-4.8%	3.1%	4.5%	5.7%	9.1%
Return on Equity	8.3%	18.8%	31.7%	25.4%	15.4%	-15.0%	10.7%	14.1%	13.8%	14.8%
ROIC	3.9%	9.7%	20.7%	18.4%	9.5%	-8.1%	5.3%	8.6%	10.2%	12.9%
Shares Out.	8	8	9	8	8	7	7	7	7	6
Revenue/Share	278.52	106.14	94.01	103.80	114.80	118.15	21.08	16.21	15.24	19.45
FCF/Share	14.89	5.67	16.05	11.69	-0.54	-4.97	14.75	12.22	3.72	4.84

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