



H.B. Fuller (FUL)

Updated September 26th, 2019 by Aristofanis Papadatos

Key Metrics

Current Price:	\$46	5 Year CAGR Estimate:	5.9%	Volatility Percentile:	66.1%
Fair Value Price:	\$45	5 Year Growth Estimate:	5.0%	Momentum Percentile:	19.1%
% Fair Value:	102%	5 Year Valuation Multiple Estimate:	-0.4%	Growth Percentile:	40.4%
Dividend Yield:	1.4%	5 Year Price Target	\$57	Valuation Percentile:	59.2%
Dividend Risk Score:	A	Retirement Suitability Score:	B	Total Return Percentile:	39.0%

Overview & Current Events

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

Given the \$2.4 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 Adecol 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 late September, H.B. Fuller reported (9/25/19) financial results for the third quarter of fiscal 2019. Revenues decreased 5.8% and organic revenues decreased 3.3%. While the company maintained its strong momentum in engineering adhesives, it was negatively affected by poor trends in construction adhesives and the economic slowdown in some regions. The gross margin climbed from 28.4% to 28.8% thanks to lower material costs and synergies from past acquisitions but adjusted earnings-per-share remained flat at \$0.86 and missed the analysts' consensus by \$0.04. H.B. Fuller has missed the analysts' earnings-per-share consensus in 6 of the last 9 quarters.

Moreover, management lowered its guidance for adjusted earnings-per-share from \$3.10-\$3.30 to \$2.95-\$3.05 and adjusted EBITDA from \$455-\$465 to \$440-\$445 million this year due to a slowdown in global industrial production. We have thus lowered our guidance for the earnings-per-share of this year from \$3.20 to \$3.00.

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	\$3.00	\$3.83
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
Shares¹	48.7	49.2	49.5	49.8	50.2	50.3	50.1	50.1	50.2	52.0	51.5	55.0

There is a high degree of uncertainty in the business of H.B. Fuller 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 a whole decade. 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	15.3	15.0
Avg. Yld.	1.6%	1.3%	1.4%	1.1%	1.0%	1.0%	1.3%	1.3%	1.1%	1.2%	1.4%	1.5%

¹ In millions

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H.B. Fuller is currently trading at a price-to-earnings ratio of 15.3. While the historical average earnings multiple of the stock is 16.7, we assume a fair price-to-earnings ratio of 15.0 due to the challenges facing the business and the high cyclicality of the stock. If the stock trades at our fair valuation level in five years, it will incur a 0.4% annualized drag in its returns due to the contraction 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%	21.3%	21.8%

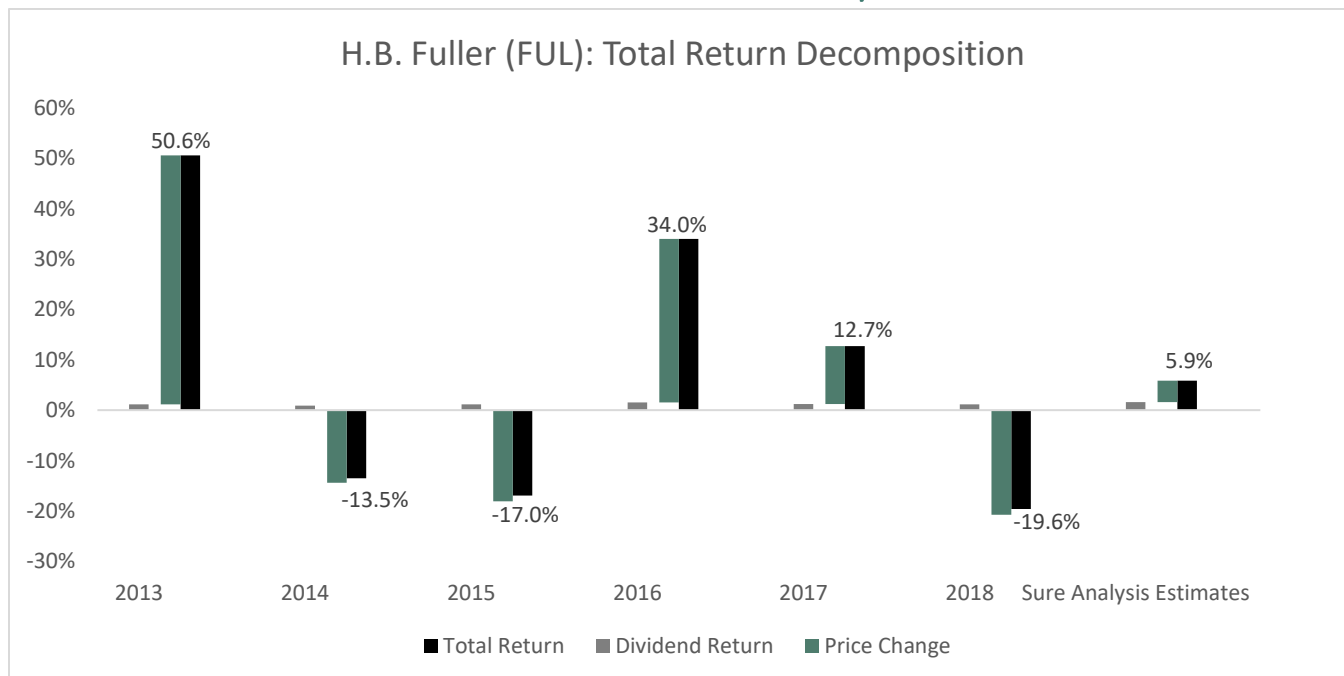
Due to the acquisition of Royal Adhesives & Sealants, interest coverage has plunged to an almost decade low of 2.1. However, management has repeatedly confirmed that it will be using a major portion of free cash flows to reduce debt. The company reduced its debt by \$204 million last year and is on track to reduce it by another \$260 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. Moreover, H.B. Fuller is highly leveraged to economic growth and hence the stock is likely to outperform the market in rallies and underperform the market in rough periods. The company is notably 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 a decade, investors should take this risk factor into account, especially given the company's increased leverage.

Final Thoughts & Recommendation

H.B Fuller has volatile earnings record, it is vulnerable to economic downturns and has lackluster business performance due to a slowdown in the industrial production in some regions. We expect the stock to offer just a 5.9% average annual return over the next five years. Given the low yield and the downside risk in the event of a recession, income-oriented investors should pass here. We rate the stock as a hold for those not in need of the stock's income.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	1235	1257	1444	1886	2047	2104	2084	2095	2306	3041
Gross Profit	371	358	404	517	570	533	568	606	605	837
Gross Margin	30.1%	28.5%	28.0%	27.4%	27.9%	25.3%	27.3%	28.9%	26.2%	27.5%
SG&A Exp.	264	264	291	358	350	362	371	408	477	582
D&A Exp.	47	39	39	57	62	70	75	78	87	145
Operating Profit	107	95	113	138	196	150	170	198	128	255
Operating Margin	8.7%	7.5%	7.8%	7.3%	9.6%	7.1%	8.2%	9.5%	5.6%	8.4%
Net Profit	84	71	89	126	97	50	87	122	59	171
Net Margin	6.8%	5.6%	6.2%	6.7%	4.7%	2.4%	4.2%	5.8%	2.6%	5.6%
Free Cash Flow	49	40	55	73	6	-110	152	132	86	185
Income Tax	37	20	31	30	40	34	56	49	10	-6

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	1100	1153	1228	1786	1873	1869	2042	2056	4373	4175
Cash & Equivalents	100	133	155	200	155	78	119	142	194	151
Accounts Receivable	204	221	217	320	331	341	365	351	474	486
Inventories	117	122	116	209	222	251	249	247	372	356
Goodwill & Int. Ass.	245	240	242	488	483	452	567	572	2338	2213
Total Liabilities	506	519	518	1008	943	979	1169	1118	3321	3023
Accounts Payable	109	102	104	163	202	174	178	163	268	273
Long-Term Debt	214	251	232	520	493	575	723	703	2452	2248
Shareholder's Equity	591	632	705	778	930	890	873	938	1051	1152
D/E Ratio	0.36	0.40	0.33	0.67	0.53	0.65	0.83	0.75	2.33	1.95

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	7.7%	6.3%	7.5%	8.3%	5.3%	2.7%	4.4%	5.9%	1.8%	4.0%
Return on Equity	14.8%	11.6%	13.3%	16.9%	11.3%	5.5%	9.8%	13.4%	6.0%	15.5%
ROIC	10.5%	8.4%	9.8%	11.2%	7.1%	3.4%	5.7%	7.5%	2.3%	5.0%
Shares Out.	48.7	49.2	49.5	49.8	50.2	50.3	50.1	50.1	50.2	52.0
Revenue/Share	25.14	25.34	28.96	37.26	40.03	41.06	40.54	40.85	44.67	58.51
FCF/Share	0.99	0.80	1.11	1.44	0.12	-2.15	2.96	2.58	1.66	3.56

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

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