



H&R Block Inc. (HRB)

Updated September 25th, 2019 by Samuel Smith

Key Metrics

Current Price:	\$24	5 Year CAGR Estimate:	7.2%	Volatility Percentile:	72.1%
Fair Value Price:	\$25	5 Year Growth Estimate:	2.6%	Momentum Percentile:	36.4%
% Fair Value:	97%	5 Year Valuation Multiple Estimate:	0.6%	Growth Percentile:	15.9%
Dividend Yield:	4.4%	5 Year Price Target	\$28	Valuation Percentile:	71.8%
Dividend Risk Score:	C	Retirement Suitability Score:	B	Total Return Percentile:	53.1%

Overview & Current Events

H&R Block, Inc. is a \$4.8 billion global consumer tax services provider. It offers comprehensive tax return preparation through approximately 12,000 company owned and franchised H&R Block locations around the world. H&R Block also offers tax software. The company generates annual revenue of more than \$3 billion, and prepared over 23 million tax returns in fiscal 2018.

HRB company announced financial results for the fiscal 2020 first quarter on June 11th, 2019. The company posted a loss of \$0.72 per share, unchanged year-over-year. This is also typical for the company, which almost always loses money during its fiscal Q1 due to the seasonality of its tax business. Meanwhile, revenue grew year-over-year by 4%. The company also reiterated its guidance for the full year.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$1.25	\$1.69	\$1.81	\$1.75	\$1.53	\$1.96	\$2.98	\$2.40	\$2.40	\$2.40	\$2.48	\$2.82
DPS	\$0.70	\$0.80	\$0.80	\$0.80	\$0.80	\$0.84	\$0.92	\$0.98	\$1.00	\$1.02	\$1.06	\$1.20
Shares¹	292.1	272.6	274.2	275.3	220.5	207.2	209.3	207.0	207.0	207.0	207.0	207.0

By acquiring Wave Financial, H&R Block has added a boost to its otherwise murky growth outlook. Poor customer retention has prompted the company to engineer a turnaround. Broadly speaking, the operating environment for tax preparation is changing. While there will always be a need for tax preparation, the Trump administration has expressed a desire to greatly simplify the tax code. A much more simplified tax system could mean less demand for H&R Block's higher-margin services. In addition, earnings growth could be negatively impacted by the continued adoption of online or do-it-yourself tax software such as TurboTax. H&R Block has had to act on price and also invest in its own software services to meet the needs of a changing marketplace. These forces are expected to weigh on H&R Block's earnings growth, both this fiscal year and moving forward. That being said, Wave Financial will give the company more opportunities to grow in the small business sector, an area less likely to be impacted by a simplified personal income tax code.

As a result of the Wave Financial acquisition, we expect 2.6% annual earnings growth over the next five fiscal years.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	13.7	12.5	10.6	12.5	11.5	16.1	18.4	21.2	11.6	9.1	9.7	10.0
Avg. Yld.	2.8%	3.3%	4.2%	4.5%	4.1%	2.8%	2.5%	2.5%	3.7%	3.4%	4.4%	4.3%

In the past 10 years, H&R Block shares traded for an average price-to-earnings ratio of 13.7. However, earnings growth is slowing as disruption from online tax filing software is eating into H&R Block's market share and pricing power. Based on this, we view 10 times earnings as a good estimate of fair value, which is roughly where the stock trades at currently.

¹ Share count in millions

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.



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Expansion of the price-to-earnings ratio is expected to add 0.6% to the annual returns for H&R Block if mean reversion were to occur over the next 5 years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	44.4%	56.0%	47.3%	44.2%	45.7%	52.3%	42.9%	30.9%	40.8%	41.7%	42.7%	42.6%

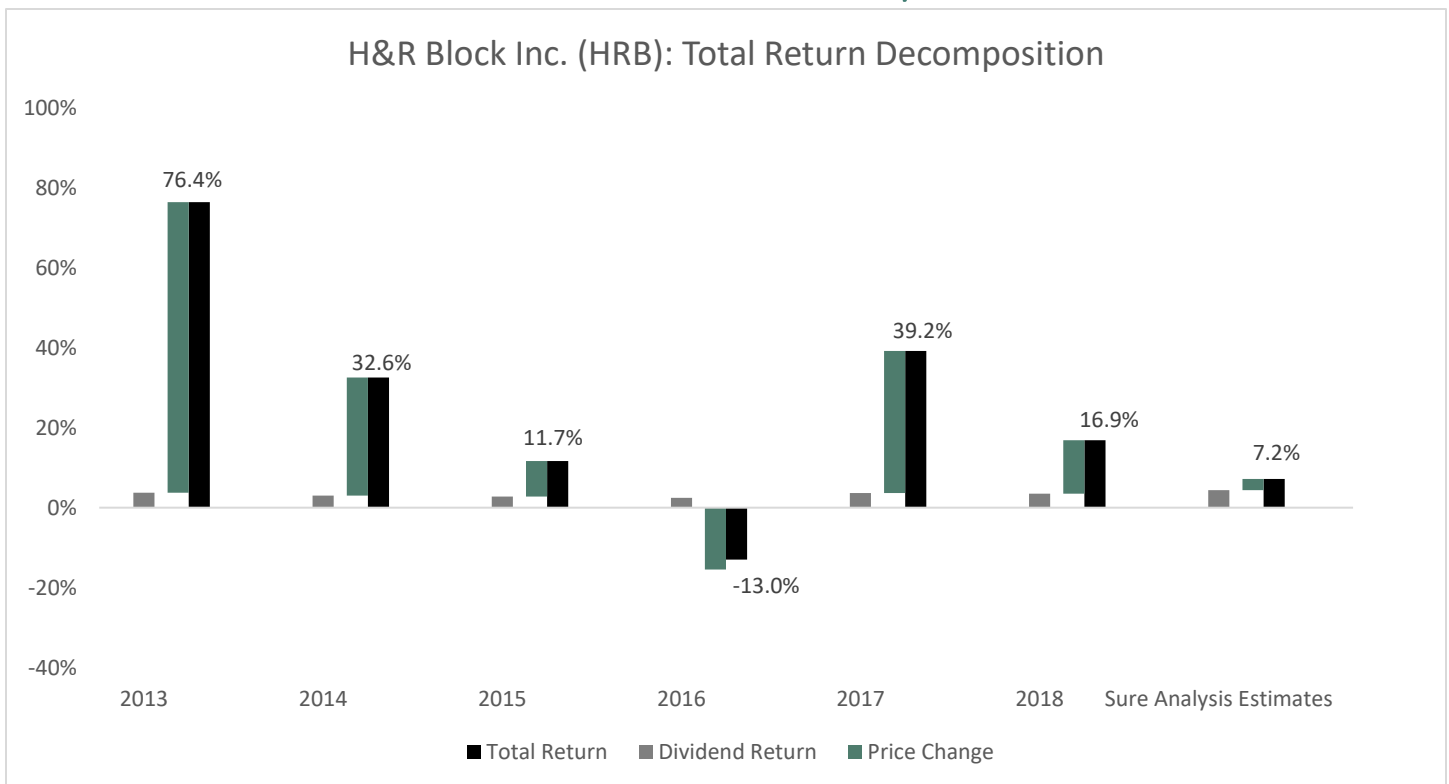
H&R Block scores fairly well when it comes to safety and quality metrics. The company has a large amount of debt, but also generates strong interest coverage. It also has a payout ratio well below 50%, which indicates the dividend is secure. H&R Block has paid quarterly dividends consecutively since the company went public in 1962.

H&R Block benefits from durable competitive advantages. It is the leading brand in the tax preparation industry, and provides a necessary service to taxpayers. H&R Block remained profitable each year during the Great Recession, and the company should be expected to remain profitable if and when another recession occurs in the United States.

Final Thoughts & Recommendation

H&R Block has a number of favorable qualities as a business. It has a leading brand in its industry and has a highly profitable business model. This allows the company to return cash to shareholders through share repurchases and dividends. However, H&R Block is in the middle of a turnaround. It needs to invest significantly to adapt to a more challenging operating climate. This will inhibit the company's growth over the next five years. H&R Block has expected returns of 7.2% per year stemming from its 4.4% dividend yield, 0.6% expected annual multiple expansion, and 2.6% expected annual earnings-per-share growth rate. Given the ongoing uncertainty facing the industry and the integration risk posed by the recent acquisition of Wave Financial, we downgrade the stock to a hold at current valuation levels.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	3752	2945	2894	2906	3024	3079	3038	3036	3160	3095
Gross Profit	1284	1168	972	1161	1202	1210	1353	1392	1420	1338
Gross Margin	34.2%	39.7%	33.6%	40.0%	39.7%	39.3%	44.5%	45.8%	44.9%	43.2%
SG&A Exp.	631	529	378	373	361	367	719	676	668	722
D&A Exp.	127	122	104	92	116	160	174	182	183	167
Operating Profit	652	639	574	771	818	795	633	716	752	616
Operating Margin	17.4%	21.7%	19.8%	26.5%	27.1%	25.8%	20.8%	23.6%	23.8%	19.9%
Net Profit	479	406	266	434	475	474	374	409	613	423
Net Margin	12.8%	13.8%	9.2%	14.9%	15.7%	15.4%	12.3%	13.5%	19.4%	13.7%
Free Cash Flow	497	450	280	384	663	503	445	463	751	511
Income Tax	295	235	230	237	267	256	186	208	42	100

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	5234	5208	4650	4538	4694	4515	2847	2694	3141	3300
Cash & Equivalents	1804	1678	1944	1748	2185	2007	897	1011	1545	1572
Accounts Receivable	327	282	129	131	125	122	109	88	16	21
Goodwill & Int. Ass.	1208	1214	704	719	792	874	905	901	882	862
Total Liabilities	3794	3758	3324	3274	3137	2682	2824	2755	2747	2758
Accounts Payable	757	618	567	524	222	231	260	217	252	250
Long-Term Debt	1966	1930	1041	907	906	506	1492	1494	1496	1493
Shareholder's Equity	1441	1450	1326	1264	1557	1833	23	-61	394	542
D/E Ratio	1.36	1.33	0.78	0.72	0.58	0.28	64.59	-24.54	3.80	2.76

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	9.0%	7.8%	5.4%	9.4%	10.3%	10.3%	10.2%	14.8%	21.0%	13.1%
Return on Equity	33.7%	28.1%	19.2%	33.5%	33.7%	27.9%	40.3%		368%	90.4%
ROIC	16.1%	12.0%	9.3%	19.1%	20.5%	19.7%	19.4%	27.7%	36.9%	21.5%
Shares Out.	292.1	272.6	274.2	275.3	220.5	207.2	209.3	207.0	207.0	207.0
Revenue/Share	11.26	9.51	9.69	10.59	10.96	11.11	12.11	14.18	15.03	14.97
FCF/Share	1.49	1.45	0.94	1.40	2.40	1.82	1.77	2.16	3.57	2.47

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

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