HNI Corporation (HNI)

Updated February 20th, 2020 by Nathan Parsh

Key Metrics

Current Price:	$41	**5 Year CAGR Estimate:**	9.5%	**Market Cap:**	$1.74 billion
Fair Value Price:	$44	**5 Year Growth Estimate:**	5.5%	**Ex-Dividend Date:**	2/21/2020
% Fair Value:	93%	**5 Year Valuation Multiple Estimate:**	1.4%	**Dividend Payment Date:**	3/2/2020
Dividend Yield:	3.0%	**5 Year Price Target**	$58	**Years Of Dividend Growth:**	9
Dividend Risk Score:	C	**Retirement Suitability Score:**	C	**Last Dividend Increase:**	3.4%

HNI Corporation was founded in 1944 as an office furniture manufacturer. The company continues to be a leader in that space as it has expanded its portfolio of brands and added a full array of hearth products including fireplaces, inserts and stoves. HNI generates about $2.3 billion in annual revenues.

On 2/19/2020, HNI reported earnings results for the fourth quarter and full year. The company earned $1.12 per share, which was $0.07 above estimates and an increase of 15.5% from the prior year. Revenue increased 3% to $616 million, but was $10 million lower than expected. For the year, adjusted earnings-per-share 7.5% to $2.59 while revenue declined 0.5% to $2.25 billion year-over-year.

Organic growth for the fourth quarter was 3.9%. Gross margins improved 60bps due to higher pricing and productivity, which was partially offset by lower volumes and higher input costs. SG&A expenses were down 50bps. Office Furniture sales increased 4.6%, with organic growth of 5.9%. An improvement in pricing, productivity and lower expenses offset a decrease in volumes, higher input costs and unfavorable product mix. Sales for Hearth Products were lower by 1.1% for the quarter due to lower volumes. For 2019, Office Furniture sales were lower by 0.5% while Hearth Products decreased 0.4%. HNI expects adjusted earnings-per-share of $2.60 to $2.90 on revenue of $2.3 billion to $2.35 billion for 2020.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$0.87	$1.05	$1.12	$1.43	$1.97	$2.58	$2.62	$1.97	$2.41	$2.59	***$2.75***	***$3.59***
DPS	$0.86	$0.92	$0.95	$0.96	$0.99	$1.05	$1.09	$1.14	$1.18	$1.22	***$1.22***	***$1.50***
Shares[1]	45	45	45	45	44	44	44	45	44	43	***43***	***41***

Because of HNI's extreme cyclicality, earnings-per-share have been volatile over the past decade. Importantly, the trend has been up, but growth has been anything but linear. Revenue growth has averaged -1% in the past decade but if we exclude the Great Recession, that number moves to 4% annually.

We maintain our earnings-per-share growth estimate of to 5.5% per year through 2025. Our growth estimate is made up of low-single-digit revenue growth, flat to slightly higher margins, and share repurchases. Again, these results may not occur in a linear fashion, but if the company is able to see a reversal in slowing in the office furniture segment, HNI looks setup for further growth. Margins should also improve in 2020 as the closing of the small office furniture business is lapped, but the impact will be relatively small.

We see the dividend continuing to rise as well, given HNI's track record of returning excess cash to shareholders. HNI increased its dividend by 3.4% for the 6/3/2019 payment. We forecast dividends per share of $1.50 or so in five years.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	31.5	24.3	23.7	25.0	19.7	18.7	16.7	21.1	15.8	14.5	***14.9***	***16.0***
Avg. Yld.	3.1%	3.6%	3.6%	2.7%	2.5%	2.2%	2.5%	2.7%	3.0%	3.3%	***3.0%***	***2.6%***

[1] In millions of shares

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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HNI's price-to-earnings multiple has moved around a lot, which is something you'd expect for a cyclical stock. We are maintaining our 2025 target price-to-earnings ratio from our previous report of 16. The share price is up $3, or 7.9% since our 10/23/2019 report. Based on the current price and earnings estimates for 2020, HNI trades with a P/E ratio of 14.9. We are therefore forecasting a 1.4% tailwind to annual total returns from a rising valuation over time. Shares offer a current yield matches the 10-year average yield of 3.0%. We expect the share price to grow more quickly than the dividend payment in the coming years, and the yield to fall back to 2.6% as a result.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	111%	86%	84%	66%	49%	40%	41%	56%%	49%	47%	***44%***	***42%***

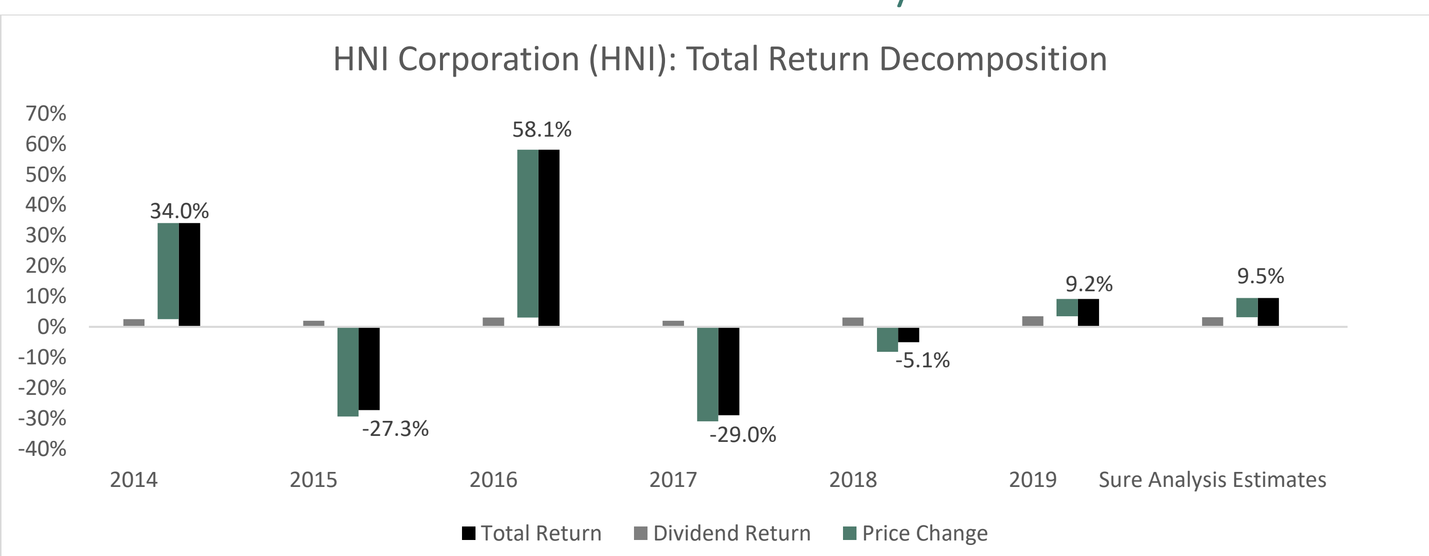
HNI's quality metrics have been somewhat volatile during the past decade but again, its results are expected to be as such. Its balance sheet has looked very much the same in terms of leverage at around 60% debt financing and excluding 2009, its interest coverage has been more than sufficient. The payout ratio has also been relatively low, and we see it moving slightly lower over time as earnings growth outpaces dividend growth by a small margin; this also allows for increased safety of the dividend during the next downturn. The somewhat troubling trend stems from gross margins, which have been weakening since 2016. Efficiency efforts and the closing of the small office furniture business should help. However, it certainly bears watching in the coming quarters for any signs of weakness.

HNI's competitive advantage is its scale in the office furniture business, as well as its long operating history and track record with customers. HNI has some of the most recognizable brands in the sector but that doesn't save it from recessions; the next time a recession hits there will almost undoubtedly be a sizable downswing in HNI's earnings.

Final Thoughts & Recommendation

Following fourth quarter and full-year results, HNI Corporation is expected to offer a total annual return of 9.5% through 2025, down from our prior estimate of 9.7%. The company's business segments saw a slight decline for the year, but the fourth quarter saw growth from Office Furniture. Shares trade with a low valuation and offer a decent dividend. HNI is also forecasting top and bottom-line growth for 2020. We have increased our 2025 price target $5 to $58 due to guidance for the current year. We've moved HNI from buy to hold as total returns are strong, but cyclicality of earnings introduces risk for shareholders.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	1,687	1,833	2,004	2,060	2,223	2,304	2,203	2,176	2,258	2,247
Gross Profit	586	639	689	715	784	847	835	784	835	834
Gross Margin	34.7%	34.9%	34.4%	34.7%	35.3%	36.8%	37.9%	36.0%	37.0%	37.1%
SG&A Exp.	518	554	600	607	649	672	668	672	691	680
D&A Exp.	59	46	43	47	57	58	69	73	75	77
Operating Profit	67	85	90	109	135	175	167	112	144	154
Operating Margin	4.0%	4.6%	4.5%	5.3%	6.1%	7.6%	7.6%	5.2%	6.4%	6.8%
Net Profit	27	46	49	64	61	105	86	90	93	111
Net Margin	1.6%	2.5%	2.4%	3.1%	2.8%	4.6%	3.9%	4.1%	4.1%	4.9%
Free Cash Flow	68	103	85	86	55	58	104	6	123	152
Income Tax	17	24	29	33	44	52	43	(19)	25	32

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	998	1,052	1,077	1,135	1,239	1,264	1,330	1,392	1,402	1,453
Cash & Equivalents	99	73	42	65	34	29	36	23	77	52
Accounts Receivable	190	204	213	229	240	243	229	259	255	275
Inventories	69	102	94	90	122	125	118	156	157	163
Goodwill & Int. Ass.	314	335	375	381	279	431	511	491	463	446
Total Liabilities	589	632	656	698	825	787	829	877	839	868
Accounts Payable	124	159	189	200	224		202	236	221	
Long-Term Debt	200	181	155	151	198	190	214	277	250	175
Shareholder's Equity	408	419	420	436	415	477	501	514	563	584
D/E Ratio	0.49	0.43	0.37	0.35	0.48	0.40	0.43	0.54	0.44	0.30

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	2.7%	4.5%	4.6%	5.8%	5.2%	8.4%	6.6%	6.6%	6.7%	7.7%
Return on Equity	6.5%	11.1%	11.7%	14.9%	14.4%	23.7%	17.5%	17.7%	17.3%	19.3%
ROIC	4.4%	7.6%	8.3%	11.0%	10.3%	16.5%	12.4%	11.9%	11.6%	14.1%
Shares Out.	45	45	45	45	44	44	44	45	44	43
Revenue/Share	36.82	40.12	43.74	44.82	48.77	50.71	48.43	48.53	50.94	51.66
FCF/Share	1.48	2.26	1.84	1.87	1.21	1.28	2.28	0.13	2.77	3.51

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