



# Williams-Sonoma Inc. (WSM)

Updated March 19<sup>th</sup>, 2020 by Eli Inkrot

## Key Metrics

<b>Current Price:</b>	\$30	<b>5 Year CAGR Estimate:</b>	16.9%	<b>Market Cap:</b>	\$2.4B
<b>Fair Value Price:</b>	\$46	<b>5 Year Growth Estimate:</b>	4.0%	<b>Ex-Dividend Date:</b>	04/23/20
<b>% Fair Value:</b>	67%	<b>5 Year Valuation Multiple Estimate:</b>	8.5%	<b>Dividend Payment Date:</b>	05/29/20
<b>Dividend Yield:</b>	6.3%	<b>5 Year Price Target</b>	\$55	<b>Years Of Dividend Growth:</b>	14
<b>Dividend Risk Score:</b>	C	<b>Retirement Suitability Score:</b>	C	<b>Last Dividend Increase:</b>	11.6%

## Overview & Current Events

Williams-Sonoma is a specialty retailer that operates home furnishing and houseware brands such as Williams-Sonoma, Pottery Barn, West Elm, Rejuvenation, Mark & Graham and others. Williams-Sonoma operates traditional brick-and-mortar retail locations but also sells its goods through e-commerce and direct-mail catalogs. Williams-Sonoma was founded in 1956, is headquartered in San Francisco, and currently trades with a market capitalization of \$2.4 billion.

On March 17<sup>th</sup>, 2020 Williams-Sonoma announced that the company will temporarily close all of its stores as a precautionary measure to combat the spread of the coronavirus. The company plans to reopen its stores on April 2<sup>nd</sup>, while e-commerce sites will remain open.

On March 18<sup>th</sup>, 2020 Williams-Sonoma announced Q4 and fiscal year 2019 results for the period ending February 2<sup>nd</sup>, 2020. (Williams-Sonoma's fiscal year ends the Sunday closest to January 31<sup>st</sup>.) For the quarter comparable brand revenue grew 7.6%, led by a 13.9% increase from West Elm. Diluted earnings-per-share totaled \$2.10 compared to \$1.93 in the prior year's quarter. For the year Williams-Sonoma generated \$5.9 billion in revenue, at the high end of previous guidance, led by 6.0% comparable brand growth. Earnings-per-share equaled \$4.49, compared to \$4.05 previously, while adjusted earnings-per-share equaled \$4.84 - up from \$4.46 in 2018 - above guidance of \$4.65 to \$4.80.

Williams-Sonoma has temporarily suspended its 2020 guidance due to the uncertainty surrounding the coronavirus but did note that the company targets mid-to-high single-digit revenue growth over the long-term.

## Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
<b>EPS</b>	\$1.83	\$2.22	\$2.54	\$2.82	\$3.24	\$3.37	\$3.41	\$3.52	\$4.05	\$4.49	<b>\$3.50</b>	<b>\$4.26</b>
<b>DPS</b>	\$0.55	\$0.73	\$0.88	\$1.24	\$1.32	\$1.40	\$1.48	\$1.56	\$1.72	\$1.92	<b>\$1.92</b>	<b>\$2.34</b>
<b>Shares<sup>1</sup></b>	105	100	98	94	92	90	87	84	79	79	<b>79</b>	<b>70</b>

Williams-Sonoma has a solid growth history. Since 2010, the company has grown earnings-per-share by an average compound rate of over 10% per annum. However, this is skewed somewhat, as recent results have been aided significantly by a lower tax rate. Stripping away this benefit, the company has been able to improve in the mid-single digits. This mirrors the type of cautious growth expectation, 4% annually, that we are anticipating from this point.

Unlike many other retailers, Williams-Sonoma has been able to increase its profits through the last couple of years, which is, among other factors, due to its consistent revenue growth. Thanks to its robust Omni-channel sales strategy, Williams-Sonoma has established a strong e-commerce business. As online sales continue to outpace company-wide revenue growth, Williams-Sonoma will become even more of an online retail company in the coming years.

This strategy will be tested in both the short-term and long-term. In the short-term the coronavirus poses a significant challenge. We have significantly reduced our earnings expectation for this year given the temporarily closure of stores and will revisit this expectation as we learn more. Share repurchases have traditionally been a growth driver for the

<sup>1</sup> In millions.

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bottom-line and may continue to help moving forward, especially with a depressed share price. However, conservation of capital in the short-term is presently more pressing.

## Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	15.8	16.6	15.8	19.4	20.8	22.2	15.5	14.1	14.0	13.7	8.7	13.0
Avg. Yld.	1.9%	2.0%	2.2%	2.3%	2.0%	1.9%	2.8%	3.1%	3.0%	3.1%	6.3%	4.2%

Williams-Sonoma has an interesting valuation history, with a typical multiple in the mid-teens coupled with occasional bouts of a 20+ earnings multiple. Taking into consideration the company's past performance, growth prospects, balance sheet and current situation, we believe a low-teens multiple is a fair starting baseline for the security. This could be too ambitious if the company's growth rate deteriorates, but we have accounted for this somewhat in the lower earnings expectations above. With today's valuation under 9 times earnings, this implies significant potential valuation upside.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	30%	33%	35%	44%	41%	42%	43%	44%	42%	43%	55%	55%

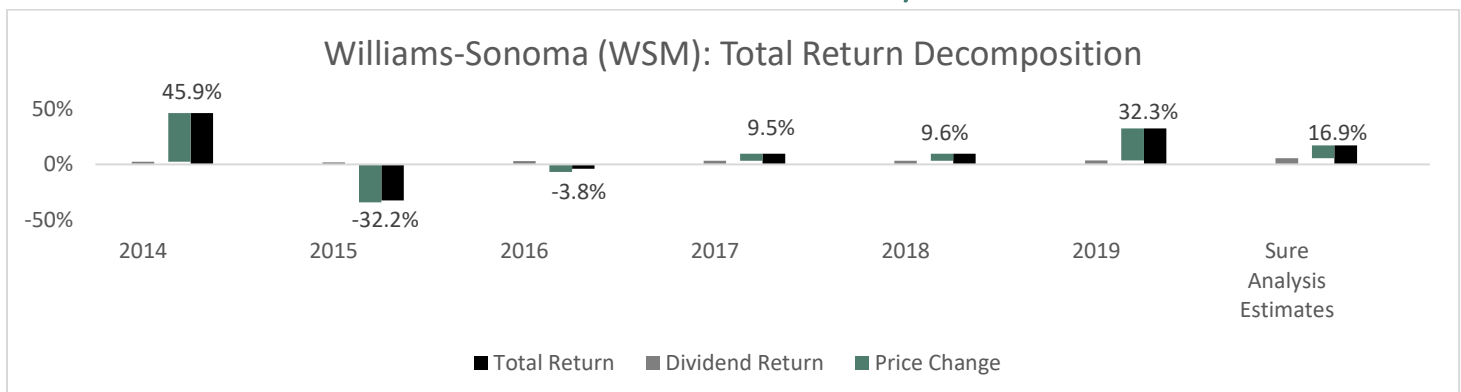
Williams-Sonoma's competitive advantage lies in its unique product portfolio and successful move to the online space. Still, the company competes against formidable foes including traditional brick-and-mortar home improvement retailers such as Home Depot and Lowe's, and e-commerce players such as Amazon. Results have been solid in the last decade, but we caution that the company's business model is quite cyclical, as consumers tend to avoid discretionary items during economic downturns. During the last recession Williams-Sonoma posted earnings-per-share of \$1.76, \$0.28, \$0.72 and \$1.83 during the 2007 through 2010 stretch while the dividend was held steady and ultimately increased.

Williams-Sonoma operates a relatively asset-light business model relative to other retailers, thanks to a high portion of online sales. As of the most recent report the company held \$432 million in cash, \$1.8 billion in current assets and \$4.1 billion in total assets against \$1.6 billion in current liabilities and \$2.8 billion in total liabilities.

## Final Thoughts & Recommendation

Shares have declined an exceptional -55% since our last report. Williams-Sonoma has transformed itself into an Omni-channel retailer with a large e-commerce presence, which will be tested in quick order. We caution that Williams-Sonoma's earnings are not very recession-resilient. Still, due to the materially lower share price, we are forecasting 16.9% annual total return potential, stemming from 4% growth, the 6.3% starting dividend yield and a valuation tailwind. Shares earn a buy rating, acknowledging that there is likely to be a great deal of near-term uncertainty.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Revenue</b>	3504	3721	4043	4388	4699	4976	5084	5292	5672	5898
<b>Gross Profit</b>	1374	1460	1592	1704	1801	1844	1883	1932	2101	2139
<b>Gross Margin</b>	39.2%	39.2%	39.4%	38.8%	38.3%	37.1%	37.0%	36.5%	37.0%	36.3%
<b>SG&amp;A Exp.</b>	1050	1078	1183	1252	1298	1356	1411	1478	1665	1673
<b>D&amp;A Exp.</b>	145	131	134	150	162	168	173	183	189	188
<b>Operating Profit</b>	323	382	409	452	502	489	473	454	436	466
<b>Operating Margin</b>	9.2%	10.3%	10.1%	10.3%	10.7%	9.8%	9.3%	8.6%	7.7%	7.9%
<b>Net Profit</b>	200	237	257	279	309	310	305	260	334	356
<b>Net Margin</b>	5.7%	6.4%	6.4%	6.4%	6.6%	6.2%	6.0%	4.9%	5.9%	6.0%
<b>Free Cash Flow</b>	294	161	159	260	257	341	327	310	396	421
<b>Income Tax</b>	123	145	153	174	193	178	167	193	96	101

## Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Total Assets</b>	2132	2061	2188	2337	2330	2417	2477	2786	2813	4054
<b>Cash &amp; Equivalents</b>	628	503	425	330	223	194	214	390	339	432
<b>Accounts Receivable</b>	42	46	63	60	67	79	89	90	107	112
<b>Inventories</b>	513	553	640	813	888	978	978	1062	1125	1101
<b>Goodwill &amp; Int. Ass.</b>	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	85	85
<b>Total Liabilities</b>	873	806	879	1081	1106	1219	1229	1582	1657	2818
<b>Accounts Payable</b>	228	218	259	405	397	447	454	459	527	521
<b>Long-Term Debt</b>	9	7	5	4	2	0	0	299	300	300
<b>Shareholder's Equity</b>	1259	1255	1309	1256	1225	1198	1248	1204	1156	1236
<b>D/E Ratio</b>	0.01	0.01	0.00	0.00	0.00	0.00	0.00	0.25	0.26	0.24

## Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Return on Assets</b>	9.5%	11.3%	12.1%	12.3%	13.2%	13.1%	12.5%	9.9%	11.9%	10.4%
<b>Return on Equity</b>	16.2%	18.8%	20.0%	21.7%	24.9%	25.6%	25.0%	21.2%	28.3%	29.8%
<b>ROIC</b>	16.1%	18.7%	19.9%	21.7%	24.8%	25.6%	25.0%	18.9%	22.6%	23.8%
<b>Shares Out.</b>	105	100	98	94	92	90	87	84	82	79
<b>Revenue/Share</b>	32.00	34.91	40.01	44.43	49.36	54.03	56.83	61.48	68.88	74.45
<b>FCF/Share</b>	2.69	1.51	1.57	2.63	2.70	3.70	3.66	3.60	4.81	5.31

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

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