NACCO Industries (NC)

Updated August 5th, 2020 by Nathan Parsh

Key Metrics

Current Price:	$23	**5 Year CAGR Estimate:**	13.1%	**Market Cap:**	$165.2 million
Fair Value Price:	$36	**5 Year Growth Estimate:**	1.0%	**Ex-Dividend Date:**	8/28/2020[1]
% Fair Value:	64%	**5 Year Valuation Multiple Estimate:**	9.4%	**Dividend Payment Date:**	9/15/2020[2]
Dividend Yield:	3.3%	**5 Year Price Target**	$38	**Years Of Dividend Growth:**	2
Dividend Risk Score:	C	**Retirement Suitability Score:**	C	**Last Dividend Increase:**	1.3%

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 produces annual revenues of $141 million in normalized conditions. The company has been very active in purchasing and spinning off a wide variety of businesses in its history. 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 reported earnings results for the second quarter on 8/5/2020. Earnings-per-share declined $0.28, or 25%, from the previous year. Revenue decreased 4.4% to $21.6 million. A 13% decrease in total coal deliveries impacted results for the second quarter. Unconsolidated volumes were down 13% while the smaller consolidated operations were lower by 11%. Unconsolidated coal is easier to acquire because it is found among loose materials where consolidated coal is found among solid rock. Partially offsetting volume declines was an increase in pricing of coal. Expenses were down 7.5% and operating profit improved 3.2%. NACCO Industries now expects coal deliveries and operating profit for 2020 to decline compared to the previous year. Limestone deliveries decreased more than 9%, but revenues were up more than 12%. This division entered into an agreement last quarter to become the exclusive contract miner for lithium in a northern Nevada. Construction will begin in 2021 with the production of lithium products to begin in 2023. Mineral Management revenues declined 76% due to royalty income generated by gas wells during 2018 and 2019. The company said that the COVID-19 pandemic hasn't impacted results yet, but could if higher natural gas inventories lead to lower prices. We have lowered our EPS estimate for 2020 to $4.00 from $5.00 as coal revenues are expected to be lower than the previous year.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$9.53	$14.86	$5.02	$5.79	$3.98	$3.13	$4.32	$4.14	$5.00	$5.66	***$4.00***	***$4.20***
DPS	$2.09	$2.12	$1.88	$1.00	$1.02	$1.05	$1.07	$0.98	$0.66	$0.76	***$0.77***	***$1.05***
Shares[3]	8	9	8	8	7	7	7	7	7	7	***7***	***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. Although NACCO has shown negative growth since 2012 and volatile earnings-per-share since then, we are maintaining our projected growth of 1% due to expected improvements in limestone deliveries for the current year.

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[1] Estimated ex-dividend date

[2] Estimated dividend payment date

[3] 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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NACCO Industries increased its dividend by 1.3% for 6/15/2020 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 $1.05 in dividends-per-share by 2025.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	8.9	6.2	18.4	10.0	13.8	16.8	14.5	18.2	8.7	8.3	***5.8***	***9.0***
Avg. Yld.	2.5%	2.3%	2.0%	1.7%	1.9%	2.0%	1.7%	1.3%	1.8%	1.6%	***3.3%***	***2.8%***

Shares of NACCO Industries have decreased by $6, or 20.7%, since our 5/9/2020 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 5.8x earnings. Investors are just not willing to pay for a company that has an issue growing earnings consistently. NACCO Industries needs to prove it can reliably grow earnings-per-share before it reaches its 5-year historical averages. We maintain our 2025 P/E target of 9 due to weakness in certain businesses. If achieved, this would add 9.4% in annual returns over the next five years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

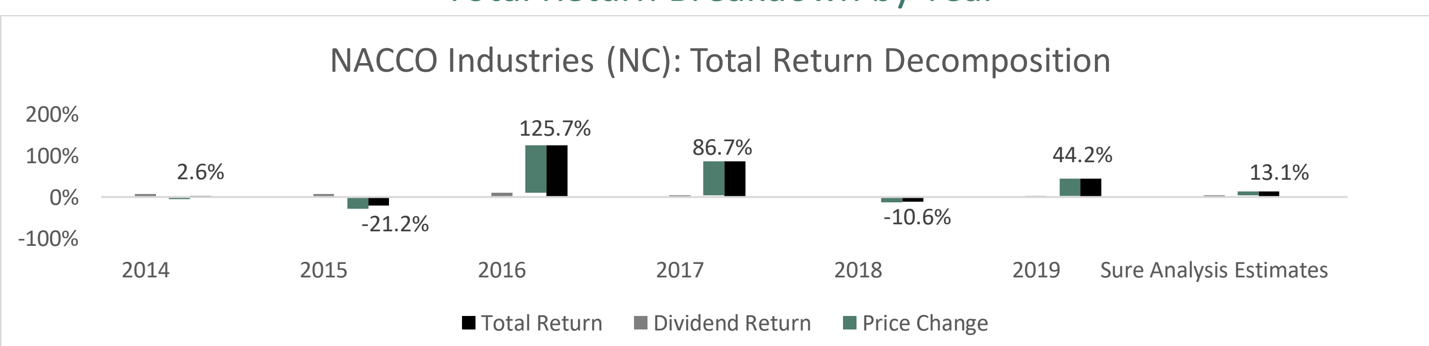
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	22%	14%	38%	17%	26%	34%	25%	24%	13%	13%	***19%***	***25%***

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. 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 second quarter results, NACCO Industries is expected to return 13.1% annually through 2025, up from 12.7% previously. NACCO Industries once again saw lower coal deliveries and lime stone deliveries also declined. The company did lower expenses for the quarter. We have lowered our 2025 price target $9 to $38 due to lowered earnings-per-share estimates. We continue to stress that only investors with a higher tolerance for risk consider purchasing NACCO Industries as the company has had a very volatile earnings history. We rate a speculative buy.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	886	790	873	933	897	148	111	105	135	141
Gross Profit	246	210	226	221	185	(11)	12	17	30	31
Gross Margin	27.8%	26.5%	25.9%	23.7%	20.6%	-7.6%	10.9%	16.1%	22.1%	22.1%
Operating Profit	49	17	11	16	(20)	(55)	(39)	(34)	(24)	(27)
Operating Margin	5.5%	2.1%	1.3%	1.8%	-2.2%	-37.1%	-35.2%	-32.7%	-17.4%	-19.0%
Net Profit	80	162	109	44	(38)	22	30	30	35	40
Net Margin	9.0%	20.5%	12.4%	4.8%	-4.3%	14.9%	26.7%	29.0%	25.7%	28.1%
Free Cash Flow	47	135	98	(4)	(38)	104	84	26	34	28
Income Tax	16	33	16	11	(38)	(10)	(10)	1	7	4

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	1,658	1,809	776	810	771	655	668	390	377	445
Cash & Equivalents	262	154	140	95	61	52	69	102	85	123
Accounts Receivable	426	101	149	153	181	114	21	35	29	22
Inventories	447	161	169	184	190	165	29	30	31	40
Goodwill & Int. Ass.	60	58	70	60	67	63	46	44	41	38
Total Liabilities	1,210	1,232	495	512	559	454	448	170	126	155
Accounts Payable	415	94	127	133	134	100	11	10	9	10
Long-Term Debt	392	148	178	184	248	170	80	50	11	25
Shareholder's Equity	447	576	281	298	211	201	220	219	251	289
D/E Ratio	0.88	0.26	0.63	0.62	1.17	0.85	0.36	0.23	0.04	0.09

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	5.1%	9.3%	8.4%	5.6%	-4.8%	3.1%	4.5%	5.7%	9.1%	9.6%
Return on Equity	18.8%	31.7%	25.4%	15.4%	-15.0%	10.7%	14.1%	13.8%	14.8%	14.7%
ROIC	9.7%	20.7%	18.4%	9.5%	-8.1%	5.3%	8.8%	10.6%	13.1%	13.8%
Shares Out.	8	9	8	8	7	7	7	7	7	7
Revenue/Share	106.14	94.01	103.80	114.80	118.15	21.08	16.21	15.24	19.45	20.12
FCF/Share	5.67	16.05	11.69	(0.54)	(4.97)	14.75	12.22	3.72	4.84	4.01

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