Harley-Davidson Inc. (HOG)

Updated November 14th, 2020 by Samuel Smith

Key Metrics

Current Price:	$34	**5 Year CAGR Estimate:**	-0.5%	**Market Cap:**	$5.2B
Fair Value Price:	$25	**5 Year Growth Estimate:**	3.7%	**Ex-Dividend Date:**	12/3/20
% Fair Value:	136%	**5 Year Valuation Multiple Estimate:**	-6.0%	**Dividend Payment Date:**	12/18/20
Dividend Yield:	0.2%	**5 Year Price Target**	$30	**Years Of Dividend Growth:**	0
Dividend Risk Score:	D	**Retirement Suitability Score:**	F	**Last Dividend Increase:**	N/A

Overview & Current Events

Since 1903, Harley Davidson has been making American-style motorcycles. They take pride in being the pioneers of the style of bikes they manufacture and finance the sale of. Harley Davidson also makes and sells parts, accessories, merchandise and maintenance/repair services. Harley Davidson has a current market capitalization of $5.2 billion. The company's dividend history has been good except for the last recession, when the dividend was cut from $1.29 in 2008 to $0.40 in 2009. This change came as their earnings per share fell from $3.77 in 2008 to $1.11 in 2009. As their motorcycles are mainly luxury items, Harley Davidson's sales are significantly impacted by economic downturns.

Harley-Davidson reported Q3 results on 10/27/2020. Non-GAAP EPS came in at $1.05 and GAAP EPS came in at $0.78. Revenue plunged by 9.9% year-over-year to $964.03 million. Gross margin was at 29.8% of sales compared to the 27.2% consensus. The challenging business environment prompted management to restructure the company according to a 5-year plan, which aims to reduce business complexity, and streamline planned motorcycle models by approximately 30 percent.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$1.38	$2.34	$2.72	$3.28	$3.88	$3.62	$3.83	$3.02	$3.19	$3.04	***$1.44***	***$3.00***
DPS	$0.40	$0.48	$0.62	$0.84	$1.10	$1.24	$1.40	$1.46	$1.48	$1.50	***$0.08***	***$1.50***
Shares[1]	235.5	230.5	226.1	220.0	211.9	184.7	176.0	168.1	162.8	162.8	***162.8***	***162.8***

Harley-Davidson is using a three-pronged approach to growth development called "New Roads". They are focused on new products, broader access, and stronger dealers. In terms of new products, this past year the company premiered its first electric motorcycle. Also, 23 new physical stores were opened in Asia to expand their market. Harley-Davidson is also expanding with e-commerce, opening a storefront on Amazon and Tmall, a large Chinese e-commerce site.

That being said, the company has been hammered by the coronavirus outbreak and will likely turn in a very disappointing performance this year, which has forced them to cut their dividend this year as they seek to conserve cash and retain some of their future growth in cash flows for reinvestment in their business and balance sheet repair.

In calculating our fair value estimate and expected total return tailwind from valuation multiple expansion, we assume a normalized "earnings power" earnings-per-share of $2.50 for this year as the business has been permanently impaired to some degree by the COVID-19 disruption.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	20.7	16.4	16.9	17.8	17.1	15.5	12.9	15.6	11.9	11.5	***13.6***	***10.0***
Avg. Yld.	1.4%	1.3%	1.3%	1.4%	1.7%	2.2%	2.8%	2.8%	3.5%	4.3%	***0.2%***	***5.0%***

[1] In millions

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Given the massive headwinds facing the company, we are reducing our fair value estimate from 13 times earnings to 10 times earnings. As a result, we expect the multiple to contract in the years to come, providing a meaningful headwind to total returns. At the same time, growth in earnings per share from this year's expected sharp decline will help to offset some of this hit to total returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	29.0%	20.0%	23.0%	26.0%	28.0%	34.0%	36.0%	43.0%	46.4%	49.3%	***5.6%***	***50.0%***

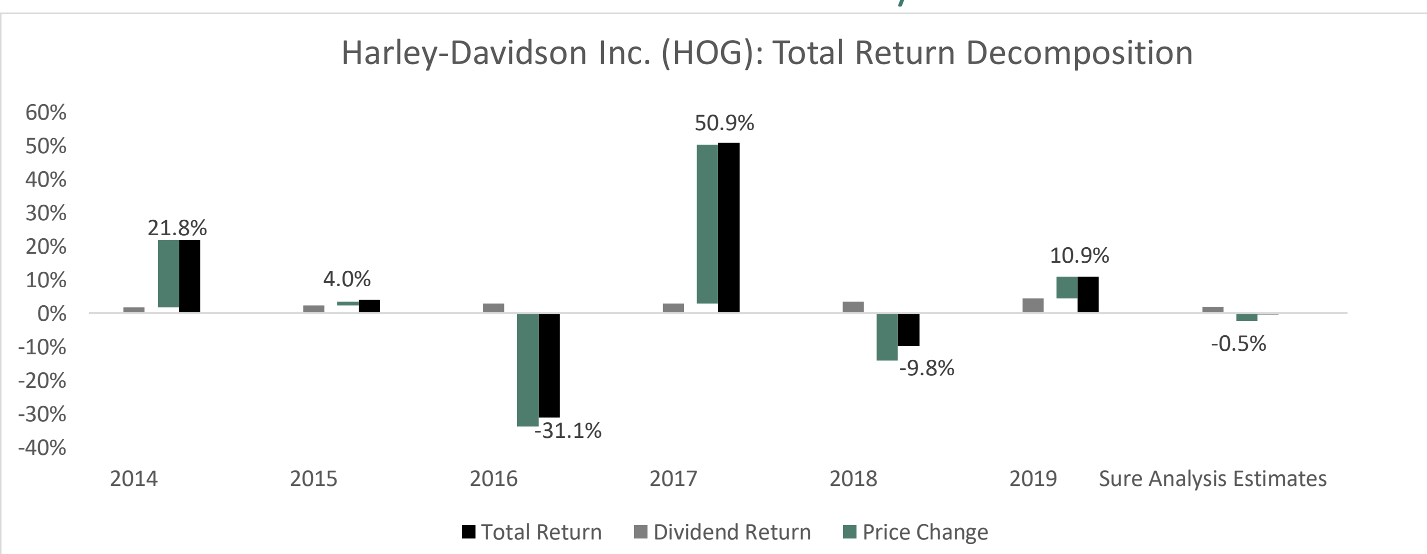
Harley-Davidson has a competitive advantage with its history, unique style and name brand recognition. Harley-Davidson has crafted their image through careful marketing such as licensing deals with TV shows such as 'Sons of Anarchy' that convey the brand's image.

During the Great Recession, Harley-Davidson was hit hard, losing 86% of its market capitalization. Earnings per share also dropped to $0.06 in 2009. Harley-Davidson has an interest coverage ratio of 28.8 and is slowly decreasing long-term debt. The largest risk to Harley-Davidson is an economic slowdown or recession. This is highly sensitive to the United States economy as 60%+ of all retail sales in recent years were in the United States. The COVID-19 recession is having a huge impact on sales and earnings, and we expect Harley-Davidson to see a slow recovery in demand.

Final Thoughts & Recommendation

As the "Rewire" restructuring takes hold and new customers come forward, HOG is expected to rebound. That being said, it will likely be a rough road fraught with risk given the unstable nature of the global economy and the company's persistently disappointing results. As a result, we expect total annualized returns for Harley-Davidson to be around -0.5% over the next half decade, and therefore view the stock as a sell. It is certainly not a stock that conservative dividend growth investors should favor as there has already been a steep dividend cut this year and concerns from the recent credit rating downgrade weigh in.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	4859	5312	5581	5900	6229	5995	5996	5647	5717	5,362
Gross Profit	1838	1976	2162	2338	2521	2477	2397	2195	2172	1,922
Gross Margin	37.8%	37.2%	38.7%	39.6%	40.5%	41.3%	40.0%	38.9%	38.0%	35.8%
SG&A Exp.	1020	1061	1111	1125	1160	1220	1214	1180	1258	1,199
D&A Exp.	255	180	169	167	179	198	210	222	265	233
Operating Profit	724	898	1029	1154	1281	1156	1046	882	807	588
Operating Margin	14.9%	16.9%	18.4%	19.6%	20.6%	19.3%	17.4%	15.6%	14.1%	11.0%
Net Profit	147	599	624	734	845	752	692	522	531	424
Net Margin	3.0%	11.3%	11.2%	12.4%	13.6%	12.5%	11.5%	9.2%	9.3%	7.9%
Free Cash Flow	922	696	612	769	914	840	918	799	992	687
Income Tax	131	245	338	380	439	398	332	342	155	134

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	9431	9674	9171	9405	9528	9973	9890	9973	10666	10528
Cash & Equivalents	1022	1527	1068	1067	907	722	760	688	1204	834
Accounts Receivable	262	1980	1973	2035	2164	2301	2361	2436	2521	2,532
Inventories	326	418	394	425	449	586	500	538	556	604
Goodwill & Int. Ass.	30	29	30	30	28	54	53	63	61	75
Total Liabilities	7224	7254	6613	6396	6619	8133	7970	8128	8892	8724
Accounts Payable	225	256	257	240	197	236	235	228	285	294
Long-Term Debt	5752	5723	5103	5259	5505	6872	6808	6988	7599	7,445
Shareholder's Equity	2207	2420	2558	3009	2909	1840	1920	1844	1774	1,804
D/E Ratio	2.61	2.36	2.00	1.75	1.89	3.74	3.55	3.79	4.28	4.13

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	1.6%	6.3%	6.6%	7.9%	8.9%	7.7%	7.0%	5.3%	5.2%	4.0%
Return on Equity	6.8%	25.9%	25.1%	26.4%	28.5%	31.7%	36.8%	27.7%	29.4%	23.7%
ROIC	1.9%	7.4%	7.9%	9.2%	10.1%	8.8%	7.9%	5.9%	5.8%	4.5%
Shares Out.	235.5	230.5	226.1	220.0	211.9	184.7	176.0	168.1	162.8	162.8
Revenue/Share	20.70	22.61	24.34	26.33	28.61	29.43	33.21	32.66	34.33	33.98
FCF/Share	3.92	2.96	2.67	3.43	4.20	4.12	5.09	4.62	5.96	4.35

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