



Lennox International (LII)

Updated February 2nd, 2023 by Nikolaos Sismanis

Key Metrics

Current Price:	\$286	5 Year CAGR Estimate:	8.0%	Market Cap:	\$9.5 B
Fair Value Price:	\$266	5 Year Growth Estimate:	8.0%	Ex-Dividend Date¹:	03/30/23
% Fair Value:	108%	5 Year Valuation Multiple Estimate:	-1.5%	Dividend Payment Date¹:	04/14/23
Dividend Yield:	1.5%	5 Year Price Target	\$390	Years Of Dividend Growth:	14
Dividend Risk Score:	C	Retirement Suitability Score:	D	Rating:	Hold

Overview & Current Events

Lennox International (LII) is a company that manufactures and sells HVAC products (heating, ventilation, and air conditioning). About 94% of sales come from North America (particularly the US and Canada), and about 6% of sales are International. The company operates through 3 segments: Residential Heating & Cooling, Commercial Heating & Cooling, and Refrigeration, which made up 68%, 19%, and 13% of 2022 sales, respectively. To preface this business, 75% of sales come from Replacements, and only 25% of sales come from New Construction – which means that this business's performance isn't directly tied to new home sales. On the Residential side of the business, the company is focused on geographic expansion of their store footprint, so they can continue to serve more households.

At the end of 2022, the business had over 260 stores and has the vision to have 350 stores by 2026. While Return on Sales has been declining on the Commercial side of the business, management expects this segment to benefit from pent-up demand and new construction. Management is looking to grow the Refrigeration business (~13% of sales) in North America and in Europe as they leverage their new digital tools and new efficiencies in their factories. Although the business is expected to have strong long-term growth, we forecast that the business will face headwinds from inflationary pressures in the near term. We expect the business to leverage its investments in e-commerce and in more streamlined factory operations as the business continues to focus on growing its higher-margin Residential Heating & Cooling business.

On January 31st, 2023, Lennox International reported Q4 2022 and full-year results for the period ending December 31st, 2022. The business earned \$2.63 in adjusted earnings-per-share in the quarter, which beat analysts' estimates by \$0.08, and was up 12% year-over-year. Revenue increased 13% year-over-year to \$1.1 billion, in-line with estimates. For fiscal 2022, revenues and adjusted earnings-per-share grew 13% and 12% to 4.7% and \$14.07, respectively. For fiscal 2023, management expects GAAP and adjusted earnings-per-share to be between \$14.25 and \$15.25. We have utilized the midpoint of this range in our estimates.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	\$3.55	\$4.28	\$5.14	\$6.95	\$7.92	\$9.42	\$11.19	\$9.94	\$12.60	\$14.07	\$14.75	\$21.67
DPS	\$0.92	\$1.14	\$1.32	\$1.58	\$1.88	\$2.43	\$2.82	\$3.08	\$3.53	\$ 4.10	\$4.24	\$7.14
Shares	49	45	43	43	42	40	39	38	37	36	36	34

Over the past 9 years, Lennox International has seen earnings-per-share grow at an average annualized rate of 16.5%, and over the past 5 years, the business has seen earnings-per-share grow at 9.4% annually. For the full fiscal year 2023, we expect the company to earn \$14.75 in earnings-per-share. We forecast that the business will continue to grow earnings-per-share at 8% annually from 2023 to 2028, which guides our 2028 earnings-per-share estimate of ~\$21.67.

¹ Estimated Date.

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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Over the past 9 years, the business has grown dividends at 18.1% annually, and over the past 5 years, the business has grown dividends at 11.8% annually. Over the next 5 years, we forecast that the business will grow dividends at 11% annually. Lennox International has grown dividend payments for 14 consecutive years.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	19.2	20.4	22.4	20.5	22.2	22.3	22.8	24.7	25.2	17.0	19.4	18.0
Avg. Yld.	1.3%	1.3%	1.1%	1.1%	1.1%	1.2%	1.1%	1.3%	1.1%	1.7%	1.5%	1.8%

Over the past 5 years, Lennox International has averaged a P/E ratio of 22.4, and over the past decade, the business has averaged a P/E ratio of 21.7. We estimate that a P/E ratio of about 18 will be fair for the business over the intermediate term as the business continues to grow earnings-per-share, while taking into account the ongoing rise in interest rates. Today, the stock offers a low dividend yield of about 1.5%, but investors might be more interested in this business's expected earnings and dividend growth.

Safety, Quality, Competitive Advantage, & Recession Resiliency

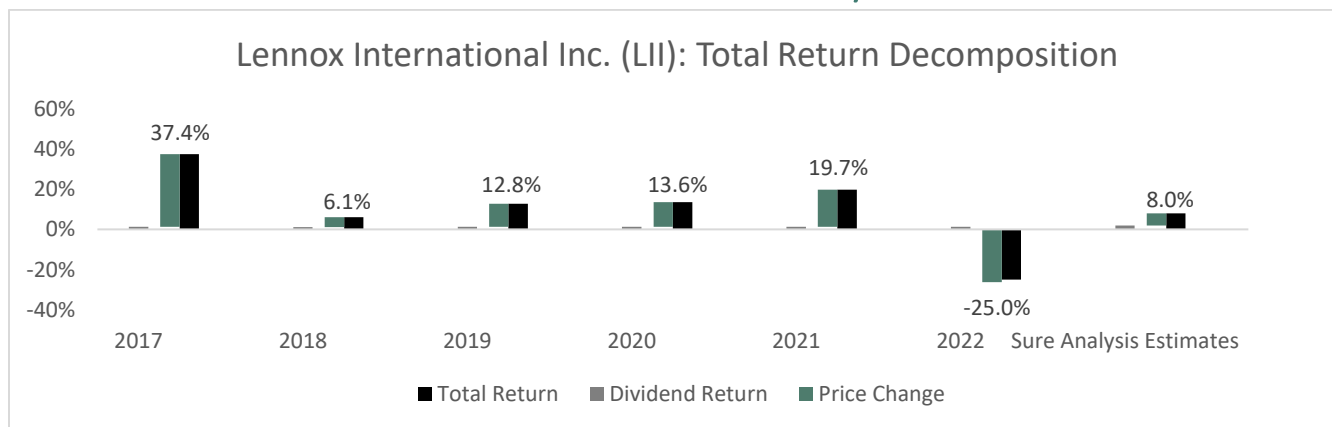
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	26%	27%	26%	23%	24%	26%	25%	31%	28%	29%	29%	33%

The business has averaged a very low payout ratio of 26% since 2013. We believe that the dividend is safe today and will continue to be over the intermediate term. The business doesn't have the strongest balance sheet because they have a lot of debt. The business has a negative shareholders' equity, but this really shouldn't be too concerning for investors, because the company has ample liquidity to pay off current liabilities, and the business can manage its long-term debt. The business has competitive advantages, including having a national presence and being a leader across many different industry verticals (including supermarkets, restaurants, discount stores, etc.) in the commercial space.

Final Thoughts & Recommendation

Lennox International offers investors an opportunity to invest in a growing business that serves an evergreen and growing market. Since the bulk of the company's revenue comes from replacing Residential HVAC systems, they are not directly tied to new home sales, and they serve an industry that will always be around. At today's price, we rate the stock as a hold because total return prospects come in at 8.0% annually over the next five years. Total return prospects are derived from earnings-per-share growth of 8% annually, a 1.5% annual valuation headwind, and the 1.5% yield.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	2,949	3,199	3,367	3,467	3,642	3,840	3,884	3,807	3,634	4,194
Gross Profit	722	861	903	947	1,077	1,125	1,111	1,080	1,040	1,188
Gross Margin	24.5%	26.9%	26.8%	27.3%	29.6%	29.3%	28.6%	28.4%	28.6%	28.3%
SG&A Exp.	507	570	574	581	621	638	608	586	556	599
D&A Exp.	55	59	61	63	58	65	66	71	73	72
Operating Profit	215	291	330	364	455	487	503	496	486	591
Op. Margin	7.3%	9.1%	9.8%	10.5%	12.5%	12.7%	13.0%	13.0%	13.4%	14.1%
Net Profit	90	172	206	187	278	306	359	409	356	464
Net Margin	3.1%	5.4%	6.1%	5.4%	7.6%	8.0%	9.2%	10.7%	9.8%	11.1%
Free Cash Flow	171	132	96	284	290	227	400	291	534	409
Income Tax	67	94	110	95	124	157	108	99	88	96

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	1,692	1,627	1,764	1,677	1,760	1,892	1,817	2,035	2,033	2,172
Cash & Equivalents	52	38	38	39	50	68	46	37	124	31
Acc. Receivable	373	408	421	423	470	507	473	478	448	508
Inventories	375	379	463	419	419	484	510	544	439	511
Goodwill & Int.	250	242	233	201	202	201	187	187	187	187
Total Liabilities	1,194	1,141	1,755	1,576	1,722	1,841	1,967	2,205	2,050	2,441
Accounts Payable	285	283	324	320	361	349	433	372	340	402
Long-Term Debt	371	383	909	741	852	989	1,022	1,138	941	1,198
Total Equity	497	485	8	101	38	50	(150)	(170)	(17)	(269)
LTD/E Ratio	0.75	0.79	108.2	7.32	22.67	19.74	(6.83)	(6.68)	(55.0)	(4.45)

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	5.3%	10.4%	12.1%	10.8%	16.2%	16.7%	19.4%	21.2%	17.5%	22.1%
Return on Equity	18.7%	35.0%	83.4%	341%	400%	697%				
ROIC	10.1%	19.8%	23.0%	21.2%	32.1%	31.7%	37.6%	44.4%	37.7%	50.1%
Shares Out.	50	49	45	43	43	42	40	39	38	37
Revenue/Share	57.38	63.22	69.29	76.04	82.76	89.71	94.50	96.63	94.15	111.84
FCF/Share	3.33	2.61	1.98	6.22	6.58	5.30	9.74	7.37	13.83	10.90

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

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