MSC Industrial Direct Co. Inc. (MSM)

Updated January 11th, 2024 by Quinn Mohammed

Key Metrics

Current Price:	$94	**5 Year CAGR Estimate:**	11.5%	**Market Cap:**	$5.3B
Fair Value Price:	$93	**5 Year Growth Estimate:**	9.0%	**Ex-Dividend Date[1]:**	01/08/2024
% Fair Value:	101%	**5 Year Valuation Multiple Estimate:**	-0.3%	**Dividend Payment Date[1]:**	01/23/2024
Dividend Yield:	3.5%	**5 Year Price Target**	$142	**Years Of Dividend Growth:**	2
Dividend Risk Score:	C	**Retirement Suitability Score:**	B	**Rating:**	Buy

Overview & Current Events

Founded in 1941 by Sid Jacobson, MSC Industrial Direct (MSM) is one the largest direct marketers and distributors of metalworking and maintenance, repair, and operations (MRO) products in North America. The company has 6 customer fulfillment centers, 10 regional inventory centers and 38 warehouses. MSM is a $5.3 billion market cap company that employees over 7,000 people.

On January 11th, 2023, MSC Industrial acquired Buckeye Industrial Supply Co, an independent metalworking distributor, as well as Tru-Edge Grinding, a custom tool manufacturer. Combined, the two companies generated $28 million in revenue in 2022.

On October 11th, 2023, MSC Industrial Direct increased its quarterly dividend by 5% to $0.83 per share.

On January 9th, 2024, MSM reported first quarter results. Net sales for the quarter came in at $954 million, a 0.4% year-over-year decline. Adjusted income from operations decreased 12.3% to $103.7 million. The adjusted operating margin was weaker than in the prior year, at 10.9% vs 12.3%. Adjusted net income decreased by 14.5% to $70.9 million and adjusted diluted EPS declined by 15.5% to $1.25 from $1.48 in the same prior year period.

Leadership reaffirmed its FY outlook, expecting adjusted operating margin to come in around 12.4% for 2024.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	$3.94	$3.78	$3.76	$4.00	$5.10	$5.20	$4.51	$4.81	$6.15	$6.29	***$5.97***	***$9.19***
DPS	$1.32	$1.60	$1.72	$1.80	$2.22	$2.76	$3.00	$3.00	$3.00	$3.16	***$3.32***	***$4.24***
Shares[2]	62	62	57	56	56	56	55	55	56	56	***56***	***50***

MSM has an average 9-year EPS compound annual growth rate of 5.3%, and a 5-year average growth rate of 4.3%. We estimate that MSM can grow forward earnings at around 9%, above its historic growth rate. The company has been able to regularly increase product prices as they see continued supplier list price movement. The company successfully completed the first chapter of its Mission Critical Program in fourth quarter 2023, and it grew over 500 basis points above the Industrial Production Index, improved adjusted operating margin by more than 200 basis points, and improved ROIC into the high teens since fourth quarter 2020. It has now announced chapter two of this program, aiming to outgrow the Industrial Production Index by at least 400 basis points, and margins of at least 20% through a business cycle. Longer term, the business aspires to achieve mid-teens operating margins and return on invested capital of 20%.

Additionally, the company states their next growth priorities include tuck-in acquisitions, such as the recent purchase of Buckeye Industrial Supply Co., and share repurchases. The emergence of Amazon is a threat; however, MSM's business is difficult to replicate, and the company has done well over the last several years to keep this threat at bay.

[1] Estimate
[2] In millions
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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Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	21.7	20.1	18.0	21.5	17.0	14.4	14.6	17.9	13.1	14.6	***15.7***	***15.5***
Avg. Yld.	1.5%	2.1%	2.5%	2.1%	2.6%	3.7%	4.4%	3.5%	3.8%	3.3%	***3.5%***	***3.0%***

Over the past nine and five years, shares of MSM have traded hands with an average P/E ratio of 17.3 and 14.9 times earnings, respectively. We credit this multiple to three basic items: a solid established business, a conservative balance sheet and a large family stake. MSM is effectively a third-generation company with the family owning about a fourth of the economic interest of MSM and having the majority of the voting power.

It is also worthwhile to note that MSM paid a special dividend in 2005, 2011, 2015 and 2020.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	34%	42%	46%	45%	44%	53%	67%	62%	49%	50%	***56%***	***46%***

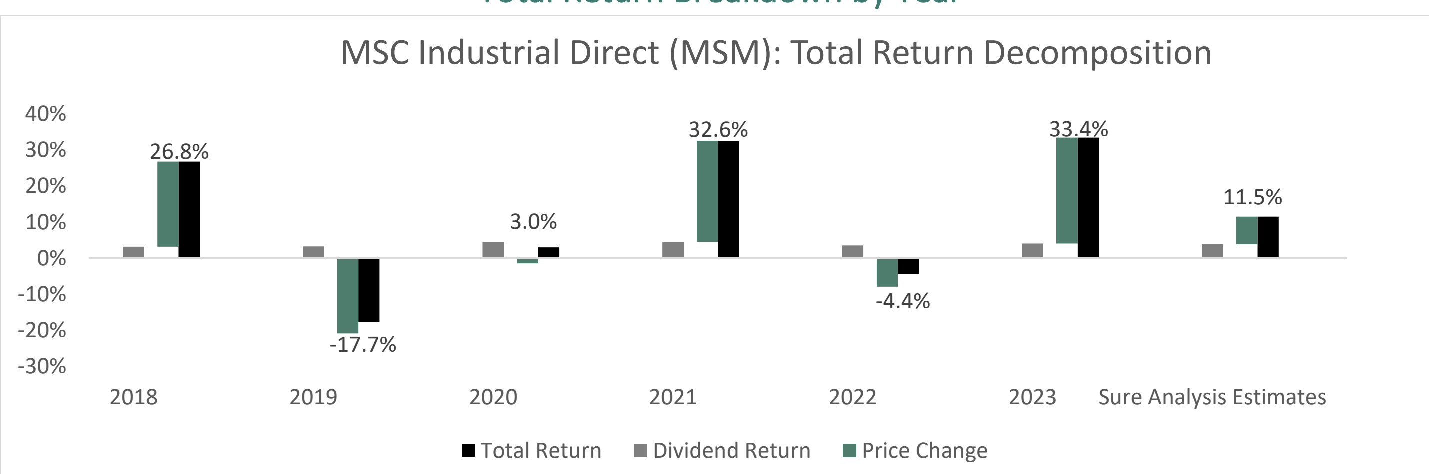
MSM's competitive advantage stems from its superior scale and execution. The company has roughly 2.4 million SKUs and boasts a strong and quick order fulfillment rate. It is true that Amazon is a formidable threat, but thus far MSM has been able to ward off attacks through its niche market relationships. A greater threat to the business is the possibility of American manufacturing, especially metalworking, moving overseas; however, this seems less and less likely.

During the last recession MSM's performance was average, posting earnings-per-share of $3.04, $2.00, $2.37, and $3.43 for the fiscal years ending 2008, 2009, 2010 and 2011, respectively. Earnings are likely to be cyclical in the future, but the overall trend has been positive. As of the last quarterly report, long-term debt stood at $294 million against adjusted operating income of around $505 million.

Final Thoughts & Recommendation

MSM is one of those companies that can easily slide under the radar unless you are directly involved in the supply chain. The general public does not see a strong brand fronting the business, so it can be difficult to conceptualize the company's competitive position. Yet due to MSM's scale, dependability, and niche relationships, the company has developed a consistent profit machine. Total returns going forward are estimated at 11.5%, which stem from the 3.5% dividend yield, 9.0% earnings-per-share growth and a potential -0.3% negative impact from valuation contraction. We rate MSC Industrial Direct as a buy at current prices.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	2787	2910	2864	2888	3204	3364	3192	3243	3692	4009
Gross Profit	1286	1317	1289	1286	1393	1432	1343	1334	1558	1643
Gross Margin	46.1%	45.2%	45.0%	44.5%	43.5%	42.6%	42.1%	41.1%	42.2%	41.0%
D&A Exp.	65	70	72	63	63	65	69	69	70	75
Operating Profit	383	380	376	379	421	407	368	339	474	492
Op. Margin	8.5%	7.9%	8.1%	8.0%	10.3%	8.6%	7.9%	6.7%	12.8%	12.3%
Net Profit	202	198	313	200	295	277	350	171	340	343
Net Margin	7.2%	6.8%	10.9%	6.9%	9.2%	8.2%	11.0%	5.3%	9.2%	8.6%
Free Cash Flow					295	277	350	171	185	607
Income Tax	143	142	141	137	77	94	82	70	111	113

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	2061	2100	2065	2099	2289	2311	2382	2462	2729	2544
Cash & Equivalents	47	38	53	16	46	32	125	41	44	50
Acc. Receivable	383	403	392	472	524	541	492	560	688	435
Inventories	450	507	444	465	518	559	543	624	716	727
Goodwill & Int.	768	743	729	744	798	794	782	795	824	829
Total Liabilities	662	767	967	874	901	827	1062	1300	1367	1052
Accounts Payable	116	114	111	121	145	160	126	186	217	226
Long-Term Debt	337	427	607	533	535	442	619	786	795	454
Total Equity	1399	1333	1098	1225	1387	1479	1315	1151	1350	1479
D/E Ratio	0.24	0.32	0.55	0.44	0.39	0.30	0.47	0.68	0.59	0.31

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	11.8%	11.1%	11.1%	11.1%	15.0%	12.6%	10.7%	9.0%	13.1%	13.0%
Return on Equity	16.9%	16.9%	19.0%	19.9%	25.2%	20.2%	18.0%	17.6%	27.2%	24.3%
ROIC	14.0%	13.2%	13.3%	13.4%	17.9%	15.0%	13.0%	11.2%	16.6%	16.7%
Shares Out.	62	62	57	56	56	56	55	55	56	56
Revenue/Share	44.71	47.33	46.88	50.69	56.50	60.60	57.37	57.82	65.87	71.32
FCF/Share	3.24	3.23	5.13	3.52	5.20	4.98	6.29	3.04	3.30	10.80

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