

Armstrong World (AWI)

\$76.96 (As of 08/14/20)

Price Target (6-12 Months): **\$65.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 07/30/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM: C

Value: D

Growth: B

Momentum: C

Summary

Armstrong World reported weak second-quarter results, wherein earnings and revenues not only missed the respective Zacks Consensus Estimate, as well as declined year over year. Lower volumes in both the Mineral Fiber and Architectural Specialties segments as a result of lower market demand due to the COVID-19 pandemic, as well as unfavorable Mineral Fiber AUV impacted the results. Although the company has been benefiting from healthcare and education verticals, and repair & remodel as well as retail and office, slowdown in key territories like New York City, Northern California and Boston hurts. Furthermore, it expects revenue to decline 10-18% for 2020, primarily due to lower volume. Shares of the company have underperformed the industry year to date.

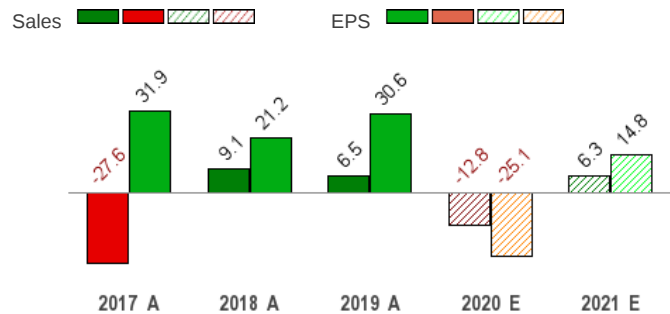
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$111.46 - \$62.03
20 Day Average Volume (sh)	548,002
Market Cap	\$3.7 B
YTD Price Change	-18.1%
Beta	1.13
Dividend / Div Yld	\$0.80 / 1.0%
Industry	Building Products - Miscellaneous
Zacks Industry Rank	Top 10% (24 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-17.6%
Last Sales Surprise	-7.5%
EPS F1 Est- 4 week change	-14.6%
Expected Report Date	NA
Earnings ESP	0.0%
P/E TTM	17.7
P/E F1	21.5
PEG F1	1.3
P/S TTM	3.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	232 E	223 E	253 E	238 E	962 E
2020	249 A	203 A	230 E	219 E	905 E
2019	242 A	272 A	277 A	247 A	1,038 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.97 E	\$0.87 E	\$1.17 E	\$1.01 E	\$4.11 E
2020	\$1.10 A	\$0.75 A	\$0.94 E	\$0.79 E	\$3.58 E
2019	\$1.10 A	\$1.27 A	\$1.38 A	\$1.11 A	\$4.78 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/14/2020. The reports text is as of 08/17/2020.

Overview

Armstrong World is a leading global producer of ceiling systems for use primarily in the construction and renovation of commercial, institutional and residential buildings. It designs, manufactures and sells ceiling systems (primarily mineral fiber, fiberglass wool, metal, wood, wood fiber, glass-reinforced-gypsum and felt) globally.

The company is based in Pennsylvania and was incorporated in 1891.

As of Dec 31, 2019, the company operated 13 active manufacturing facilities throughout the North America and one in China. Armstrong World currently operates in three reporting segments — Mineral Fiber, Architectural Specialties and Unallocated Corporate.

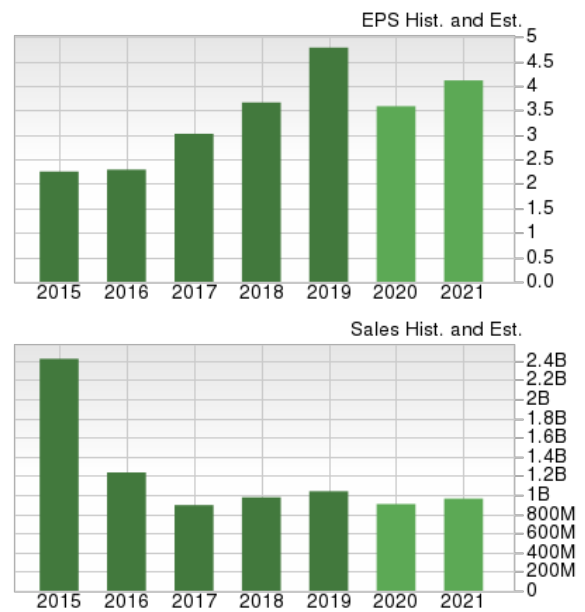
Mineral Fiber (accounting for 79.6% of 2019 revenues) produces suspended mineral fiber and soft fiber ceiling systems for use in commercial and residential settings.

Architectural Specialties (20.4%) produces and sources ceilings and walls for use in commercial settings.

The Unallocated Corporate contains cash, debt, fully funded U.S. pension plan and certain other miscellaneous balance-sheet items.

On Jun 28, 2020, Armstrong World announced the acquisition of Turf Design, Inc., a Chicago-based commercial interiors design house, and maker of custom felt ceiling as well as wall solutions.

The company ended the second quarter with \$452 million liquidity, including \$117.1 million cash and cash equivalents, and \$370 million of available capacity on the revolving credit facility. This brings total liquidity to \$487 million at second quarter-end.



Reasons To Sell:

- ▼ **COVID-19 Weighing on Results:** The recent economic slowdown owing to the COVID-19 outbreak generated significant market volatility and impacted the company's results. Armstrong World's second-quarter adjusted earnings and sales declined 40.6% and 25.3%, respectively, from a year ago mainly due to lower volumes in both Mineral Fiber and Architectural Specialties segments, thanks to COVID-19-induced lower market demand. The company's second-quarter volumes declined due to government shutdowns, project delays and distributor inventory reductions. Management highlighted that all manufacturing facilities are now operational, but many large metro areas are still weak.

Coronavirus-led weakness and soft volumes in the Mineral Fiber segment remain causes of concern.

Furthermore, the company expects sales and EPS to be down 10-18% and 20-35%, respectively, for 2020, primarily on lower volume.

- ▼ **Soft Volumes:** Volumes in the Mineral Fiber segment have been soft over the last few quarters. For second-quarter 2020, the segment sales declined 26.2%, primarily on lower volume and unfavorable average unit value ("AUV"). Also, in fourth-quarter 2019, Mineral Fiber volume was down 2% due to softness in the lower end of its product range that is directly connected to the big box channel, continued uneven R&R activity across various verticals and a weak economy in Canada. Soft volume in Mineral Fiber still remains a pressing concern, despite improvement in the same in first-quarter 2020.

Meanwhile, the company anticipates negative volume for the full year.

- ▼ **Oil Price Volatility & Continued Geopolitical Uncertainty:** International markets that are closely linked to oil, such as the Middle East will be impacted by oil price volatility and continued geopolitical uncertainty in the region.
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Risks

- **Inorganic Moves to Bolster Product Offering:** Armstrong World follows a systematic inorganic strategy to enhance its portfolio. On Jun 28, 2020, Armstrong World announced the acquisition of Turf Design, Inc., a Chicago-based commercial interiors design house and maker of custom felt ceiling as well as wall solutions. This buyout strengthens the company's design and manufacturing capabilities, as well as broadens the extensive portfolio of architectural specialties ceiling and wall solutions.

On November 2019, the company acquired MRK Industries, a manufacturer of specialty metal ceilings and walls. On Mar 4, 2019, the company acquired Architectural Components Group, Inc. ("ACGI"), a leading custom wood ceilings and walls solution provider.

The company wrapped up two additional acquisitions in Architectural Specialties, bringing the count to five in the last three years through 2019. Meanwhile, on Sep 30, 2019, it closed the divestiture of businesses and operations in Europe, the Middle East and Africa (including Russia), 'EMEA', and the Pacific Rim. That made the company an Americas-only business with minimal exposure to tariffs or the impact of coronavirus.

- **Enough Liquidity to Overcome Coronavirus Woes:** Armstrong World has been maintaining a strong liquidity position to navigate through the current environment. The company ended the second quarter with \$452 million liquidity, including \$117.1 million cash and cash equivalents, and \$370 million of available capacity on the revolving credit facility. This brings the total liquidity to \$487 million at second quarter-end. Its current cash level is sufficient to meet the short-term obligation of \$48.8 million.

The company's long-term debt of \$607.5 million was lower than \$678.5 million reported in the first quarter. First-quarter adjusted free cash flow increased sequentially to \$63 million from \$36 million reported in the first quarter of 2020 and \$55 million a year ago. Management maintained its 2020 FCF margin guidance of 22-25%, given reduced capital expenditures, working capital benefits and some tax benefits.

- **Investment in New Products:** Since its separation from the flooring business in 2016, Armstrong World has been strategically investing in new products, sales and support services, and advanced manufacturing capabilities. The company's new product launches include Sustain and Total Acoustics product families, and DESIGNFlex, which in turn fortified the Mineral Fiber category. Not just this, the company is also rolling out new digitally-enabled solutions like Revit families to its website for the DESIGNFlex products. In 2019, it introduced a digitally-enabled solution called Project Works.

Meanwhile, with the Flex line at the Marietta facility operating well, the company has automated the production of circles, triangles and trapezoids in any color. These launches have experienced extraordinary rates of adoption by architects, and the company expects the penetration of these products to continue in 2020 and beyond.

Notably, the company recently received an urgent request for products at healthcare facilities in New York City in response to the coronavirus pandemic.

Last Earnings Report

Armstrong World (AWI) Q2 Earnings & Revenues Miss Estimates

Armstrong World Industries reported disappointing second-quarter 2020 results. Earnings and revenues missed the respective Zacks Consensus Estimate, as well as declined year over year.

The company announced the acquisition of a Chicago-based commercial interiors design house and maker of custom felt ceiling as well as wall solutions — Turf Design, Inc. Notably, the acquisition will strengthen design and manufacturing capabilities, and broaden its extensive portfolio of architectural specialties ceiling as well as wall solutions.

Quarter Ending 06/2020

Report Date	Jul 28, 2020
Sales Surprise	-7.50%
EPS Surprise	-17.58%
Quarterly EPS	0.75
Annual EPS (TTM)	4.34

Earnings & Revenues Discussion

Armstrong World reported adjusted earnings of 75 cents per share, which lagged the Zacks Consensus Estimate of 91 cents by 17.6% and declined 40.6% from \$1.27 a year ago.

Net sales of \$203.2 million also lagged the consensus mark of \$220 million by 7.5% and fell 25.3% year over year. The decline was mainly due to lower volumes in both Mineral Fiber and Architectural Specialties segments due to COVID-19-induced lower market demand. Also, unfavorable Mineral Fiber AUV, driven by regional weakness in major metropolitan areas impacted by COVID-19, added to the woes.

Operational Update

Gross margin during the quarter came in at 33.4%, which contracted 460 basis points from the year-ago period. Selling, general and administrative (SG&A) expenses, as a percentage of net sales, increased a whopping 250 bps year over year to 16.2%.

Adjusted EBITDA fell 36.3% from the prior-year quarter to \$69 million, primarily due to lower volumes, partially offset by reduced SG&A expenses and improved manufacturing productivity.

Segmental Performance

Mineral Fiber: The segment's sales were down 26.2% on a year-over-year basis to \$157.9 million due to lower volume and unfavorable AUV.

Operating income also decreased 42.6% from the prior-year quarter, attributable to lower volumes, WAVE earnings and unfavorable AUV, partially offset by improved manufacturing productivity, higher Transition Service Agreement cost reimbursements, along with a reduction in incentive compensation expenses. Adjusted EBITDA also declined 34.8% from the prior-year quarter to \$62 million.

Architectural Specialties: Net sales in the segment slid 21.8% year over year to \$45.3 million due to lower demand across almost all product categories and geographies as a result of the COVID-19 pandemic.

The segment's operating profit and adjusted EBITDA decreased 54.7% and 47.9% from the year-ago level, respectively. The downside mainly stemmed from lower sales volume and additional amortization expense related to acquisitions made in 2019.

Financials

As of Jun 30, 2020, Armstrong World had cash and cash equivalents of \$117.1 million compared with \$45.3 million at 2019-end. Net cash provided by operations was \$78.7 million in past six months compared with \$47 million in the comparable prior-year period.

The company's free cash flow (on an adjusted basis) was \$63 million compared with \$55 million in the year-ago quarter.

Its board of directors authorized the buyback of additional shares of \$500 million within the existing repurchase program and extended the term until 2023.

2020 Outlook

Considering sequential market improvement and no second wave of market shutdown, the company expects sales to be down 10-18% and adjusted EBITDA margins to be more than 35% for 2020. It anticipates generating a free cash flow margin of 22-25% this year.

Valuation

Armstrong World shares are down 18.1% in the year-to-date period and 20.1% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Construction sector are up 14.1% and 6.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are up 34.9% and 21.5%, respectively.

The S&P 500 index is up 4.5% in the year-to-date period and 15.4% in the past year.

The stock is currently trading at 19.67X forward 12-month earnings, which compares to 18.48X for the Zacks sub-industry, 18.53X for the Zacks sector and 22.87X for the S&P 500 index.

Over the past five years, the stock has traded as high as 23.45X and as low as 12.4X, with a 5-year median of 16.84X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$65 price target reflects 16.62X forward 12-month earnings.

The table below shows summary valuation data for AWI

Valuation Multiples - AWI					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	19.67	18.48	18.53	22.87
	5-Year High	23.45	19.28	19.08	22.87
	5-Year Low	12.4	7.15	10.74	15.25
	5-Year Median	16.84	13.83	15.86	17.58
P/S F12M	Current	3.85	1.44	2.13	3.7
	5-Year High	4.76	3.59	2.13	3.7
	5-Year Low	0.8	0.69	1.18	2.53
	5-Year Median	2.43	0.91	1.63	3.05
EV/EBITDA TTM	Current	6.64	21.28	19.22	12.74
	5-Year High	16.26	30.62	21.26	12.85
	5-Year Low	5.6	13.63	12.43	8.25
	5-Year Median	10.94	22.84	17.93	10.91

As of 08/14/2020

Industry Analysis Zacks Industry Rank: Top 10% (24 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Lumber Liquidators Holdings, Inc. (LL)	Outperform	2
PGT, Inc. (PGTI)	Outperform	1
Gibraltar Industries, Inc. (ROCK)	Outperform	1
Simpson Manufacturing Company, Inc. (SSD)	Outperform	1
GCP Applied Technologies Inc. (GCP)	Neutral	2
Quanex Building Products Corporation (NX)	Neutral	3
Construction Partners, Inc. (ROAD)	Neutral	2
Frontdoor, Inc. (FTDR)	Underperform	5

Industry Comparison Industry: Building Products - Miscellaneous				Industry Peers		
	AWI	X Industry	S&P 500	NX	ROCK	SSD
Zacks Recommendation (Long Term)	Underperform	-	-	Neutral	Outperform	Outperform
Zacks Rank (Short Term)	5	-	-	3	1	1
VGM Score	C	-	-	A	C	D
Market Cap	3.68 B	1.51 B	23.68 B	556.32 M	2.23 B	4.48 B
# of Analysts	4	3	14	1	2	2
Dividend Yield	1.04%	0.00%	1.68%	1.89%	0.00%	0.89%
Value Score	D	-	-	A	D	F
Cash/Price	0.03	0.09	0.07	0.16	0.06	0.07
EV/EBITDA	10.12	9.10	13.36	7.21	19.95	19.87
PEG Ratio	1.31	1.96	2.99	NA	NA	NA
Price/Book (P/B)	9.14	1.86	3.22	1.72	3.14	5.01
Price/Cash Flow (P/CF)	11.97	9.63	12.82	3.61	21.29	26.48
P/E (F1)	21.37	21.63	22.06	16.96	23.19	28.73
Price/Sales (P/S)	3.77	1.34	2.51	0.64	2.04	3.79
Earnings Yield	4.65%	4.45%	4.30%	5.90%	4.30%	3.49%
Debt/Equity	1.51	0.47	0.77	0.71	0.03	0.20
Cash Flow (\$/share)	6.43	2.31	6.94	4.69	3.23	3.89
Growth Score	B	-	-	A	B	C
Hist. EPS Growth (3-5 yrs)	21.40%	20.08%	10.41%	10.72%	22.73%	22.31%
Proj. EPS Growth (F1/F0)	-25.05%	-3.28%	-6.32%	5.26%	14.92%	20.30%
Curr. Cash Flow Growth	15.31%	-3.66%	5.20%	108.85%	15.67%	-4.69%
Hist. Cash Flow Growth (3-5 yrs)	3.83%	13.97%	8.55%	28.42%	21.12%	13.26%
Current Ratio	2.04	2.04	1.33	2.93	1.73	4.32
Debt/Capital	60.13%	38.09%	44.59%	41.49%	3.32%	16.67%
Net Margin	-5.64%	2.67%	10.13%	-1.58%	7.16%	13.71%
Return on Equity	56.59%	10.82%	14.51%	10.49%	13.92%	18.50%
Sales/Assets	0.64	1.04	0.51	1.28	1.10	1.01
Proj. Sales Growth (F1/F0)	-8.80%	0.00%	-1.43%	0.00%	10.21%	3.79%
Momentum Score	C	-	-	F	D	D
Daily Price Chg	0.23%	0.00%	0.12%	0.12%	0.45%	-0.01%
1 Week Price Chg	2.01%	4.11%	2.30%	11.74%	21.62%	3.49%
4 Week Price Chg	-2.31%	6.80%	4.41%	19.69%	35.86%	17.84%
12 Week Price Chg	6.24%	23.09%	13.66%	46.46%	64.29%	37.58%
52 Week Price Chg	-18.58%	9.44%	5.80%	-0.53%	63.86%	64.77%
20 Day Average Volume	548,002	221,660	1,984,154	154,403	177,897	266,691
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-14.60%	14.55%	2.08%	0.00%	24.84%	53.86%
(F1) EPS Est 12 week change	-10.83%	21.34%	2.66%	0.00%	24.84%	53.86%
(Q1) EPS Est Mthly Chg	-24.20%	22.47%	0.94%	NA	19.88%	112.77%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	B
Momentum Score	C
VGM Score	C

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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