

Mohawk Industries (MHK)

\$96.96 (As of 08/27/20)

Price Target (6-12 Months): **\$102.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 06/22/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:A

Value: A

Growth: B

Momentum: B

Summary

Mohawk's shares have outperformed its industry so far this year. The company's dominant market share in the highly fragmented and competitive industry, acquisition strategy, and strong international presence are expected to drive growth. The firm is streamlining operations, merging facilities and removing higher-cost assets to combat cost woes. These will lower costs by \$110-120 million and boost EBITDA by 10%. Estimates for 2020 moved north over the past 30 days, depicting analysts' optimism over the company's prospects. However, visibility is low due to continuous COVID-19 spread. Again, soft U.S. ceramic market, heightened competition and tariff-related woes are pressing concerns. Mohawk's shares have underperformed the industry over the past three months.

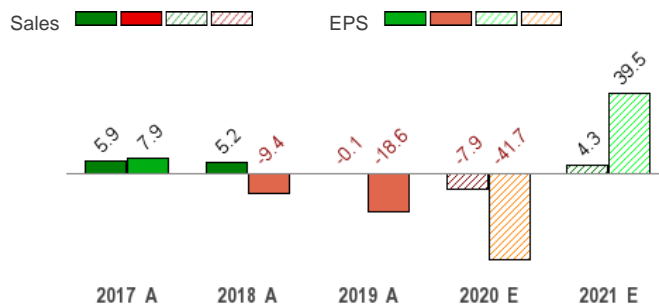
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$153.05 - \$56.62
20 Day Average Volume (sh)	799,080
Market Cap	\$6.9 B
YTD Price Change	-28.9%
Beta	1.43
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Textile - Home Furnishing
Zacks Industry Rank	Bottom 11% (224 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	562.5%
Last Sales Surprise	7.9%
EPS F1 Est- 4 week change	26.9%
Expected Report Date	10/22/2020
Earnings ESP	7.8%
P/E TTM	13.8
P/E F1	16.6
PEG F1	3.3
P/S TTM	0.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	2,416 E	2,367 E	2,531 E	2,380 E	9,575 E
2020	2,286 A	2,050 A	2,448 E	2,401 E	9,184 E
2019	2,442 A	2,584 A	2,519 A	2,425 A	9,971 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.15 E	\$1.78 E	\$2.39 E	\$2.11 E	\$8.16 E
2020	\$1.66 A	\$0.37 A	\$1.95 E	\$1.91 E	\$5.85 E
2019	\$2.13 A	\$2.89 A	\$2.75 A	\$2.25 A	\$10.04 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 08/27/2020. The reports text is as of 08/28/2020.

Overview

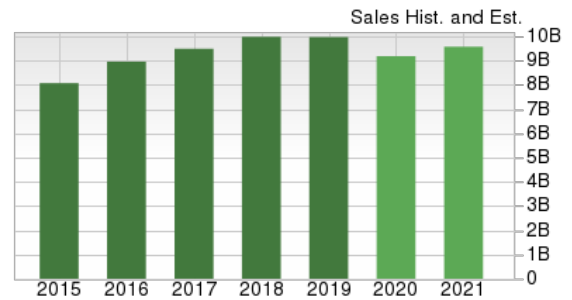
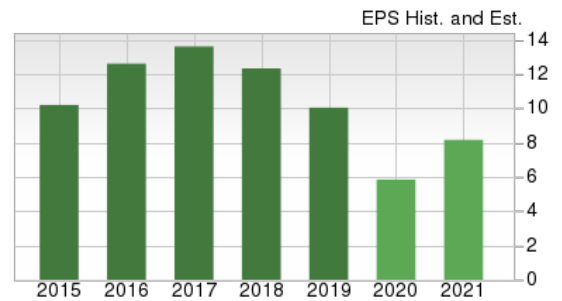
Mohawk Industries, Inc. is a leading global manufacturer of flooring products that enhance residential and commercial space. The company manufactures carpet, rugs, ceramic tile, laminate, wood, stone and vinyl flooring. It has a global presence with operations in Australia, Brazil, Canada, Europe, India, Malaysia, Mexico, New Zealand, Russia and the United States.

The company has reorganized its business into three segments — Global Ceramic, Flooring North America (Flooring NA) and Flooring Rest of the World (Flooring ROW).

Global Ceramic (accounting for 36.4% of 2019 net sales): The Global Ceramic segment includes ceramic tile, porcelain tile and natural stone operations. Some of the brands included in this segment are American Olean, Daltile, KAI, Kerama Marazzi, Marazzi and Ragno.

Flooring NA segment (38.6%): The Flooring NA segment includes North American operations of various product categories, including carpets, rugs, carpet pad, hardwood, laminate and vinyl products including LVT. The new segment combines the former Carpet segment, the North American operations of the former Laminate and Wood segment, and the North American operations of the newly acquired vinyl flooring businesses. Some of the brands in this segment include Aladdin, Bigelow, Columbia Flooring, Durkan, Horizon, IVC, Karastan, Lees, Mohawk, Pergo, Portico, QuickStep and SmartStrand.

The **Flooring ROW** segment (25%): The Flooring ROW segment includes laminate, hardwood flooring, roofing elements, insulation boards, medium-density fiberboard (MDF), chipboards, and vinyl flooring products, including LVT. The new segment combines the European and Rest of the World operations of the former Laminate and Wood segment and the European and Rest of the World operations of the vinyl flooring businesses acquired recently. Some of the brands in this segment include IVC, Moduleo, Pergo, Quick-Step and Unilin.



Reasons To Buy:

- ▲ **Strategic/Restructuring Initiatives to Boost Performance:** Over the last few quarters, Mohawk has been experiencing various headwinds like softness across the business, inflationary pressure, lower volumes and pricing concerns.

It has undertaken various strategic initiatives to improve profitability. The most significant of these initiatives are aligning ceramic production with demand in the United States, realigning its North American carpet operations, optimizing LVT manufacturing and ramping up new plant. In addition, it has been focusing on new product categories, introducing innovative product extensions and optimizing the recent buyouts. Mohawk is also investing in more sales personnel and marketing to boost its penetration in new and existing products to address ever-changing market needs. In addition, the company is streamlining operations to enhance efficiencies and leveraging automation and process enhancements to lower costs.

Although mix and competitive pressure will offset the positive impact of the price rise in the near term, the above-mentioned initiatives are likely to help the company in the upcoming quarters.

Meanwhile, the company has been undertaking business restructuring measures to boost its performance that include reducing SG&A, headcount, and lower-performing products as well as SKUs. It has also been closing less efficient operations and investing in more productive equipment. The company expects these global actions to deliver annual savings of \$110-\$120 million, with an estimated cost of \$170 million, of which cash cost is \$44 million. It will take almost the entire 2021 to complete these initiatives and capture the full benefit.

- ▲ **Diverse Acquisitions:** An opportunistic approach to acquisitions is an important part of Mohawk's growth strategy. These acquisitions broaden Mohawk's product portfolio, expand its geographic footprint and market share. During 2019, Mohawk acquired two hard surface flooring distribution companies based in the Netherlands and Czech Republic.

In 2018, Mohawk acquired leading flooring companies in Australia, New Zealand and Brazil. In Europe, it bought two flooring distributors and a specialized mezzanine company. It entered into European porcelain slab and carpet tile markets during the year. The company expanded higher-quality ceramic in Eastern Europe, and initiated sheet vinyl production in Russia along with quartz countertop manufacturing in the United States. Much of the benefits from these capital investments will be realized in 2020 and beyond, as it starts to achieve higher volume, mix and productivity.

While these acquisitions have already started contributing to the top line, Mohawk has initiated new investments to enhance its capability and introduce new products.

- ▲ **Well-Positioned in the Sector:** Mohawk is one of the largest flooring manufacturers in the global market. The company holds a dominant market share in extremely fragmented and competitive industry. In addition, the company commands a competitive advantage in the laminate flooring channel backed by the Laminate and Wood segment's industry-leading design, patented technologies and brands.

Mohawk is making higher internal investments to boost capacity and enter new markets. Although higher inflation and slowing market conditions have been grappling Mohawk over the last few quarters, it selectively invested approximately \$1.5 billion to enhance its long-term performance, primarily in new product categories and geographies, with greenfield projects and acquisitions, cost-saving initiatives and share buyback.

The largest investments during the 2017-2018 period have been the expansion of LVT in the United States and Europe; ceramic capacity increases in the United States, Mexico, Italy, Poland, Bulgaria and Russia; luxury laminate in the United States, Europe and Russia; carpet tile in Europe; sheet vinyl in Russia; countertops in the United States and Europe; and carpet and rugs in the United States.

The company is also adding unique capabilities to introduce differentiated products and anticipates higher productivity improvement in the days ahead.

- ▲ **Enough Liquidity to Tide Over COVID-19 Crisis:** As of Jun 27, 2020, the company had cash and cash equivalents of \$737.7 million (of which \$413 million was in the United States and \$324.7 million in foreign countries), higher than \$263.1 million at first quarter-end. The company's cash includes the remaining proceeds from the two bond offerings earlier this year, after paying down outstanding commercial paper. Mohawk has enough liquidity to pay the current debt of \$135 million. Meanwhile, its total debt to total capital decreased sequentially to 27% from 27.4%.

- ▲ **Strong International Presence:** Mohawk enjoys strong international presence, with higher net sales being generated outside the United States. The company has presence in Australia, Brazil, Canada, Europe, India, Malaysia, Mexico, New Zealand, and Russia. The strong international presence allows the company to capitalize on high demand in the lucrative global market.

The company is increasing utilization of new investments in the United States, Europe and Russia through more product offerings, expansion of customer base and increase in production.

Mohawk enjoys a leading position in the home furnishings industry, and its strategic acquisitions & restructuring efforts are encouraging

Reasons To Sell:

- ▼ **COVID-19 to Weigh on Near-Term Results:** While Mohawk is geographically quite diversified, the scope and suddenness of this pandemic is quite different from the housing recession in 2008-2009, which makes it difficult for manufacturers to respond to. Demand has dropped drastically across all the markets served by the company, with residential remodeling being impacted the most and DIY products having performed most impressively, as some people have started projects while staying home. Hence, given the uncertainty surrounding COVID-19, management did not provide its third-quarter EPS guidance.

Coronavirus-related disruptions, softening demand, along with stiff competition mar growth prospects

Also, the class action lawsuit/SEC investigation is likely to remain a near-term overhang on the stock. Mohawk did not divulge much on the case other than citing intentions to "vigorously defend" the charges.

- ▼ **Challenging U.S. Ceramic Market:** Mohawk's operating backdrop had remained tough throughout 2018 and 2019. Specially, the U.S. ceramic market has been impacted by a decline in product mix, soft retail demand, a stronger dollar, shift of customers to LVT and excess inventories in the channel. Recently, the United States imposed 104% tariffs on Chinese imports. Further anti-dumping duties are anticipated going forward. Mohawk expects the U.S. ceramic market to remain soft in the upcoming period. During fourth-quarter 2019, total U.S. ceramic imports declined 17%, with Chinese ceramic imports falling 90% from the year-ago period.

Mohawk's European ceramic business is also being impacted by lower market demand. Hence, the company has been reducing inventory levels, expanding product offerings and entering new categories.

Its ability to offset these pressures is hindered by continuous inflation, more competitive imports due to a stronger dollar and substitution of LVT to other alternatives. In 2019, adjusted earnings decreased 18.6% year over year. Adjusted operating margin also contracted 250 basis points from a year ago, attributed to the above-mentioned headwinds.

- ▼ **Competitive Landscape:** The flooring industry is highly competitive with a number of players (large and small), including imports, offering products in the marketplace. The company needs to make significant investments in new products, distribution network and manufacturing facilities that could impact profitability.
- ▼ **Business Sensitive to General Economic Conditions:** Mohawk's business is dependent on general economic conditions like consumer confidence, income and spending, corporate and government spending, interest rate levels plus availability of credit and demand for housing. Hence, any prolonged downturns in the United States and global economies are expected to leave a negative impact on the floor covering industry and in turn, the company's business.
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Last Earnings Report

Mohawk's Q2 Earnings and Revenues Beat Estimates

Mohawk Industries, Inc. reported solid second-quarter 2020 results, wherein earnings and revenues handily surpassed the Zacks Consensus Estimate.

As highlighted by Jeffrey S. Lorberbaum, chairman and CEO of Mohawk, "After the company's sales bottomed in April, our markets improved more than we expected, and shipments exceeded our production rates, reducing our inventories."

Mohawk reported adjusted earnings of 37 cents per share against the consensus mark of a loss of 8 cents. However, the metric declined 87.2% year over year.

Net sales of \$2 billion surpassed the consensus estimate of \$1.9 billion by 7.9% but fell 20.7% from the year-ago figure. On a constant-currency and days basis, net sales were down 19% year over year.

Operating Highlights

Adjusted gross profit of \$439.4 million was down 40.9% year over year. Adjusted selling, general and administrative expenses decreased 13.5% from the prior-year level. Adjusted operating income totaled \$35.8 million, which declined 87.1% year over year.

Segment Details

Global Ceramic: Sales in the segment totaled \$753.3 million, down 21% year over year. Also, the metric declined 19% on a constant currency and days basis. Adjusted operating income decreased to \$3.9 million from \$117.7 million a year ago due to lower volume, unfavorable price and mix, as well as COVID-19-induced shutdown.

Flooring North America: Net sales at the segment came in at \$800 million, down 19% year over year. Moreover, the segment registered adjusted operating loss of \$17.3 million for the quarter versus an operating profit of \$65.4 million a year ago. Improvement in productivity and reduction in inflation were offset by lower volume, price, mix and the COVID-19 outbreak.

Flooring Rest of the World: Net sales in the segment fell 23% year over year to \$496.4 million. On a constant-currency and days basis, sales were down 20% from the year-ago level. Adjusted operating income was \$59.1 million, down from \$105.7 million a year ago. The downside was due to lower price and mix, and volume and shutdown costs, partially offset by reduced inflation along with increased productivity.

Financial Highlights

As of Jun 27, 2020, cash and cash equivalents were \$737.7 million compared with \$128.1 million in the comparable year-ago period. For the second quarter, it generated free cash flow of almost \$500 million and issued more than \$1 billion of new bonds.

Net debt was \$1.97 billion at second quarter-end, down from \$2.46 billion in the first quarter.

Efforts to Combat COVID-19

The company has been undertaking business restructuring measures to boost its performance that include reducing SG&A, headcount, and lower-performing products as well as SKUs. It has also been closing less efficient operations and investing in more productive equipment. The company expects these global actions to deliver annual savings of \$110-\$120 million, with an estimated cost of \$170 million, of which cash cost is \$44 million. It will take almost the entire 2021 to complete these initiatives and capture the full benefit.

Third-Quarter View

Although Mohawk was unable to provide guidance for the third quarter due to uncertainties associated with the COVID-19 outbreak, it expects a significant improvement in the quarterly results from the second quarter.

The residential remodeling and new construction channels have recovered more than commercial, wherein businesses are maintaining a cautious approach to investment. Notably, its July sales were almost flat with the prior year.

Quarter Ending 06/2020

Report Date	Aug 06, 2020
Sales Surprise	7.85%
EPS Surprise	562.50%
Quarterly EPS	0.37
Annual EPS (TTM)	7.03

Valuation

Mohawk shares are down 28.9% in the year-to-date period and 16.9% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Discretionary sector are down 31% and 1.5% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is down 18.5% but the sector is up 8.2%.

The S&P 500 index is up 8.2% in the year-to-date period and 19.5% in the past year.

The stock is currently trading at 13.16X forward 12-month earnings, which compares to 11.04X for the Zacks sub-industry, 34.86X for the Zacks sector and 23.37X for the S&P 500 index.

Over the past five years, the stock has traded as high as 21.06X and as low as 5.67X, with a 5-year median of 14.91X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$102 price target reflects 13.79X forward 12-month earnings.

The table below shows summary valuation data for MHK.

Valuation Multiples - MHK					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	13.16	11.04	34.86	23.37
	5-Year High	21.06	19.41	34.86	23.37
	5-Year Low	5.67	6.86	16.13	15.25
	5-Year Median	14.91	14.67	19.86	17.58
P/S F12M	Current	0.73	0.44	2.48	3.82
	5-Year High	2.16	1.58	2.95	3.82
	5-Year Low	0.42	0.33	1.68	2.53
	5-Year Median	1.53	1.15	2.5	3.05
EV/EBITDA TTM	Current	7.59	5.69	11.38	13.27
	5-Year High	14.92	12.45	17.79	13.27
	5-Year Low	4.6	3.99	8.34	8.25
	5-Year Median	10.22	8.46	12.22	10.92

As of 08/27/2020

Industry Analysis Zacks Industry Rank: Bottom 11% (224 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
American Woodmark Corporation (AMWD)	Outperform	1
Beacon Roofing Supply, Inc. (BECN)	Outperform	3
BMC Stock Holdings, Inc. (BMCH)	Outperform	1
Fortune Brands HomeSecurity, Inc. (FBHS)	Outperform	1
FloorDecor Holdings, Inc. (FND)	Outperform	1
Culp, Inc. (CULP)	Neutral	4
SELECT INT CONC (SIC)	Neutral	3
Interface, Inc. (TILE)	Neutral	3

Industry Comparison Industry: Textile - Home Furnishing				Industry Peers		
	MHK	X Industry	S&P 500	BECN	FND	TILE
Zacks Recommendation (Long Term)	Neutral	-	-	Outperform	Outperform	Neutral
Zacks Rank (Short Term)	3	-	-	3	1	3
VGM Score	A	-	-	A	F	A
Market Cap	6.90 B	163.88 M	23.67 B	2.21 B	7.49 B	447.89 M
# of Analysts	8	2	14	7	11	2
Dividend Yield	0.00%	0.00%	1.64%	0.00%	0.00%	0.52%
Value Score	A	-	-	A	F	A
Cash/Price	0.11	0.12	0.07	0.46	0.02	0.22
EV/EBITDA	6.12	5.82	13.33	11.54	36.28	5.52
PEG Ratio	3.25	3.78	3.05	NA	2.74	NA
Price/Book (P/B)	0.87	1.07	3.18	1.31	8.81	1.73
Price/Cash Flow (P/CF)	5.10	5.10	12.81	4.82	37.80	2.92
P/E (F1)	16.55	21.50	21.68	16.84	62.92	6.71
Price/Sales (P/S)	0.74	0.44	2.50	0.32	3.63	0.36
Earnings Yield	6.02%	3.79%	4.43%	5.95%	1.59%	14.90%
Debt/Equity	0.32	0.70	0.74	1.98	1.30	2.62
Cash Flow (\$/share)	19.01	0.90	6.94	6.66	1.92	2.62
Growth Score	B	-	-	A	D	A
Hist. EPS Growth (3-5 yrs)	-3.63%	-3.24%	10.41%	5.47%	18.11%	10.83%
Proj. EPS Growth (F1/F0)	-41.78%	-25.33%	-4.94%	-15.62%	0.08%	-28.30%
Curr. Cash Flow Growth	-5.69%	-5.69%	5.22%	11.78%	30.45%	-12.37%
Hist. Cash Flow Growth (3-5 yrs)	7.62%	6.26%	8.50%	40.23%	48.52%	15.06%
Current Ratio	2.53	2.42	1.35	2.25	1.56	2.29
Debt/Capital	24.51%	38.09%	43.86%	61.58%	56.48%	72.36%
Net Margin	5.20%	1.92%	10.25%	-1.80%	7.04%	-4.44%
Return on Equity	6.40%	4.54%	14.66%	9.45%	13.31%	29.22%
Sales/Assets	0.69	1.24	0.50	1.02	0.86	0.91
Proj. Sales Growth (F1/F0)	-7.89%	-5.30%	-1.43%	-2.87%	11.06%	-16.98%
Momentum Score	B	-	-	A	D	B
Daily Price Chg	3.97%	0.00%	0.43%	-1.20%	-1.96%	5.44%
1 Week Price Chg	0.07%	0.00%	-1.45%	1.11%	4.47%	-12.81%
4 Week Price Chg	16.41%	2.45%	3.75%	5.17%	3.46%	-4.73%
12 Week Price Chg	-10.22%	12.17%	3.95%	18.57%	31.42%	-19.01%
52 Week Price Chg	-16.92%	-20.70%	2.75%	3.35%	49.95%	-30.33%
20 Day Average Volume	799,080	92,784	1,887,168	518,803	1,407,687	472,272
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	26.93%	0.00%	0.79%	13.33%	39.74%	34.12%
(F1) EPS Est 12 week change	57.07%	37.35%	3.43%	30.24%	38.66%	37.35%
(Q1) EPS Est Mthly Chg	49.94%	29.90%	0.00%	3.91%	154.67%	26.47%

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	A
Growth Score	B
Momentum Score	B
VGM Score	A

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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