

Herman Miller Inc.

NasdaqGS: MLHR

Analyst: Matthew Darcy

Sector: Industrial/Consumer

BUY

Price Target: \$38.11

Key Statistics as of 4/23/2015

Market Price:	\$28.75
Industry:	Home and Office Furniture
Market Cap:	\$1.72B
52-Week Range:	\$27.22-32.72
Beta:	1.087

Thesis Points:

- Growth assumptions can be more optimistic than Analysts' expectations
- The Company's stock is the best investment in its industry.

Company Description:

Founded in 1905, Herman Miller is a designer, manufacturer, marketer, and seller of high quality office furniture. The company is expanding its reach beyond the office, moving into markets such as residential, healthcare, and education. Their main customer is currently the US government, although no customer accounts for more than 5% of revenue. The stock has a dividend yield of 1.92%. The company has a focus on lowering fixed costs, which results in low operating leverage. They make up for this with a debt to assets ratio of 25%, which gives them financial leverage and low WACC. In the past year, the company spent 48.8 million in order to terminate their defined benefit pension plans. Its level of debt is currently at its lowest point in over 10 years.



Thesis

The office furniture market is a growing market due to an increasing number of corporate jobs. Within that industry, Herman Miller is a leading company with above average margins and inventory turnover. It is also undervalued, due to pessimistic analyst expectations for growth. These factors make Herman Miller a BUY.

The Product

Herman Millers products provide solutions for workplace design. This company invented the cubical, and has now moved on to a concept they call the living office. That is, the products can be arranged to fit any room, and any purpose. By mixing and matching various components of the furniture, the customer can create workspaces that fit their own specific needs. The company has products that work like this for office spaces as well as nurses and doctors offices. It is also foreseeable that this concept be applied to dormitories, as the company attempts to penetrate the education market.



The company also designs and produces ergonomic rolling chairs, stools, and benches, tables, accessories such as mounts for computer monitors, tablets, laptops, and power outlets, waste bins, and other miscellaneous objects needed or wanted in the workplace or at home.

Growth in the Industry

The type of labor needed in United States and other economies is continuously shifting from industrial production and process driven work towards corporate or “knowledge work” as described in the company’s 10k. This means there is an increasing need for efficient office spaces, both in the U.S. market and other growing markets.

The Business and Institutional Furniture Manufacturers Association (BIFMA) has put out a forecast for the industry which shows growth of both production and consumption.

CURRENT U.S. OFFICE FURNITURE MARKET FORECAST				
Year	Production	% Change	Consumption	% Change
2015	\$10.2 billion	+4.5 %	\$ 13.2 billion	+ 8.6 %
2016	\$10.9 billion	+6.4 %	\$ 14.5 billion	+10.0 %

Because the size of Herman Miller’s Market share, within the industry. is not expected to change, it can be assumed that increases in consumption for the industry, will be equivalent to increases in growth of Herman Miller’s Sales. These growth rates are higher than the median growth rate assumptions by analysts, which are 2.7% and 7.0% respectively. Growth is an area that can cause a significant difference between the market price and the actual value of the company.

Herman Miller against its Peers

When compared to its peers, in the home and office furniture industry, Herman Miller is contested, for best stock, by one other company. Knoll Inc. In the comparison table below, one can see that Knoll has impressive EBITDA growth, as well as, the highest operating margin, in the industry. Knoll is also very similar in size to Herman Miller, and has the second highest R&D expense to net sales.

Name	Tkr & Exch	Mkt Cap (USD)	Beta:Y-1	P/E	WACC	EBITDA ¹ 1Yr Growth LF	GM LF	OPM LF	Inv Turnover LF	R&D/Net Sales:Y
Average		1.51B	1.07	20.19	9.51%	37.89%	33.09%	4.32%	10.75	1.38%
100) HERMAN MILLER INC	MLHR US	1.74B	0.93	16.44	8.80%	13.39%	36.89%	7.24%	12.43	3.50%
101) KNOLL INC	KNL US	1.15B	1.12	19.61	9.29%	325.38%	35.76%	8.37%	5.12	1.83%
102) OKAMURA CORP	7994 JP	884.96M	0.89	17.30	7.09%	-8.69%	28.73%	1.66%	9.12	0.47%
103) HNI CORP	HNI US	2.56B	1.14	32.64	10.58%	-19.96%	35.25%	3.84%	13.62	0.00%
104) STEELCASE INC-CL A	SCS US	2.30B	1.12	21.13	9.55%	-25.14%	31.11%	4.93%	13.26	1.26%
105) KIMBALL INTERNATIONAL-BKBAL US		410.07M	1.23	14.01	11.74%	-57.66%	30.77%	-0.11%	10.94	1.24%

Knoll Inc. operates primarily in the residential furnishings industry, with a smaller line in the office furnishings industry, while Herman Miller is the opposite. Although Knoll has very impressive financials, when you look at the P/E ratio, Knoll Inc. is currently fairly valued, while Herman Miller is slightly undervalued.

This is confirmed by a more in-depth evaluation, using Economic profit, based on ROIC, and using the growth assumptions provided above. When Knoll Inc. is valued this way, the intrinsic value is \$22.85 and the Current Price is \$23.00. Herman Miller, however, is undervalued by \$4.85 with a one year target that would yield a 34% return. An overview of both valuations can be found below.

Herman Miller has a below average Beta and WACC, the highest Gross Profit Margin, above average Operating margin and inventory turnover, and the highest R&D expense as a percentage of Sales.

The large inventory turnover can be attributed to the fact that raw materials are purchased and assembled after the orders are placed. This reduces the costs of holding inventory and eliminates the risk of overproduction. Lastly, looking at R&D, this company is more likely to be successful in their growth aspirations. This is because the company will be able to innovate their products better and faster than its competitors. The company's plans for growth will be explained in more depth below.

Growth Specific to Herman Miller

Herman miller has begun growing inorganically, in order to become more of a consumer brand rather than a producer of office equipment, which resembles commodities. This requires expansion into the home furniture markets.

In 2013, they purchased a fabric designer and manufacture, Maharam Fabric Corp, for \$156 million cash. In July of 2014, the company purchased Design Within Reach, a marketer and seller of both residential and commercial furnishings, for \$154 million cash. When companies make acquisitions in cash rather than stock, it indicates that the company believes its stock is undervalued. The closing price of MLHR stock on the day of this announcement was \$29.98. It is \$28.75 today.

Neither, of these companies, operated outside the U.S. and Herman Miller does. Therefore these brands may be able to expand geographically, with the help of Herman Miller.

The company's strategic goals for expansion are increasing foreign revenue, and penetrating the education, healthcare, and residential markets. They also want the company to become more desirable, as a consumer brand, rather than an industrial product. They believe this will help them penetrate the residential market more effectively. This is the driving reason behind their more recent acquisitions.

Herman Miller has plans for organic growth as well. By pumping 3.5% of its revenue into R&D, the company is able to come up with new designs and concepts, such as living office, which help keep them relevant. The company's ability to stay ahead of the competition, is what helps keep their profit margins higher than average.

Summary

When looking at the office furniture industry, Herman Miller is the best stock. This is not only due to its high margins and inventory turnover. The most important thing is valuation of the company. At a market price of \$28.75 with a target price of \$38.1, this company will yield its investors over 30%. The company is also low risk, with a beta near 1, a focus on reduced fixed costs, and inventory made to order. High return and low risk makes this company a BUY.

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Herman Miller Inc.	mlhr	Analyst Matthew Darcy	Current Price \$28.75	Intrinsic Value \$33.63	Target Value \$38.11	Divident Yield 2%	Target Return 1-y Return: 34.48%	BULLISH			
General Info		Peers		Market Cap.		Management					
Sector	Industrials	HNI Corp.	\$2,282.44	Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014			
Industry	Commercial Services and Supplies	Steelcase Inc.	\$2,261.63	Walker, Brian	Chief Executive Officer, President :	\$3,295,935	\$3,784,692	\$3,721,203			
Last Guidance	Mar-18-2015	Knoll, Inc	\$1,126.45	Lok, Andrew	Executive Vice President and Presi	\$1,210,524	\$1,116,786	\$1,052,348			
Next earnings date	6/24/2015	Okamura Corp.	\$889.10	Pullen, Curtis	Executive Vice President and Presi	\$1,043,041	\$1,179,299	\$1,093,787			
Market Data		Kimball International, Inc.	\$408.51	Goeman, Donald	Executive Vice President of Resear	\$636,515	\$856,654	\$929,036			
Enterprise value	\$1,998.83	Current Capital Structure		Bylsma, Gregory	Chief Operating Officer of Hermar	\$875,404	\$1,156,230	\$1,057,955			
Market Capitalization	\$1,713.33	Total debt/market cap	19.03%	Stutz, Jeffrey	Chief Financial Officer and Executi	\$0	\$0	\$0			
Daily volume	0.38	Cost of Borrowing	6.24%	Historical Median Performance							
Shares outstanding	59.59	Interest Coverage	4.2x					mlhr	Peers	Industry	All U.S. firms
Diluted shares outstanding	59.79	Altman Z	4.22	Growth	3.7%	3.0%	3.4%	7.4%			
% shares held by institutions	85.99%	Debt Rating	D	ROIC	13.8%	6.2%	15.6%	14.3%			
% shares held by insiders	1.12%	Levered Beta	0.99	NOPLAT Margin	6.7%	3.6%	7.3%	10.4%			
Short interest	1.51%	WACC (based on market value weights)	7.37%	Revenue/Invested Capital	2.07	1.74	2.14	1.37			
Days to cover short interest	2.56										
52 week high	\$32.72										
52-week low	\$27.22										
5y Beta	1.35										
6-month volatility	21.88%										
Past Earning Surprises			Revenue	EBITDA	Norm. EPS						
Last Quarter	0.2%	6.1%	8.8%								
Last Quarter-1	0.6%	1.3%	-1.9%								
Last Quarter -2	0.6%	0.8%	0.0%								
Last Quarter -3	-1.4%	1.7%	8.7%								
Last Quarter -4	-0.5%	3.4%	0.0%								
Proforma Assumptions			Forecast								
			Period	Rev. Growth	Adj. Op. Cost/Rev	Invested Capital	NOPLAT Margin	ROIC	WACC		
Money market rate as of today			LTM	6.0%	88.3%	\$1,080.31	7%	13.8%	7.4%		
Annual increase (decrease) in interest rates			NTM	8.6%	88.3%	\$1,117.64	7%	15.7%	7.6%		
Yield Spread acceleration			NTM+1	10.0%	88.4%	\$1,138.41	7%	16.1%	7.7%		
Marginal Tax Rate			NTM+2	5.3%	88.4%	\$1,156.26	7%	16.4%	7.8%		
Risk-Free rate			NTM+3	3.6%	88.4%	\$1,172.48	7%	16.8%	8.0%		
Tobin's Q			NTM+4	4.3%	88.4%	\$1,186.55	7%	17.1%	8.1%		
Op. Cash/Rev.			NTM+5	3.7%	88.5%	\$1,200.34	7%	17.5%	8.2%		
Growth in PPE			NTM+6	3.5%	88.5%	\$1,214.02	7%	17.9%	8.4%		
Long term Growth			NTM+7	3.4%	88.5%	\$1,227.48	7%	18.2%	8.5%		
Base Year Unlevered Beta			NTM+8	3.3%	88.5%	\$1,234.43	7%	18.6%	8.6%		
Long term Unlevered Beta			Continuing Period	3.3%	88.6%	\$222.97	7%	13.5%	8.7%		
Valuation							Pricing Model				
Period	Invested Capital x (ROIC-WACC)	Total Debt	Other non-interest bearing claims	Shares Outstanding	DCF (Weight = 100%)	Relative (Weight = 0%)	Distress (Weight = 0%)	Weighted Average Price Per Share			
LTM	\$0.00	\$326.00	-\$11.96	59.59	\$34.29	\$38.03	\$31.40	\$34.29			
NTM	\$87.98	\$326.00	-\$176.40	59.59	\$38.89	\$46.03	\$36.04	\$38.89			
NTM+1	\$93.86	\$326.00	-\$262.89	59.59	\$40.63	\$50.57	\$37.81	\$40.63			
NTM+2	\$97.45	\$326.00	-\$357.23	59.59	\$42.48	\$54.20	\$39.59	\$42.48			
NTM+3	\$101.76	\$326.00	-\$457.98	59.59	\$44.36	\$58.06	\$41.41	\$44.36			
NTM+4	\$106.04	\$326.00	-\$565.31	59.59	\$46.38	\$61.99	\$43.25	\$46.38			
NTM+5	\$110.09	\$326.00	-\$676.67	59.59	\$48.13	\$65.87	\$45.18	\$48.13			
NTM+6	\$114.03	\$326.00	-\$792.59	59.59	\$50.03	\$69.80	\$47.53	\$50.03			
NTM+7	\$118.01	\$326.00	-\$919.70	59.59	\$52.01	\$73.94	\$50.08	\$52.01			
NTM+8	\$122.16	\$326.00	-\$1,052.60	59.59	\$53.64	\$78.21	\$52.66	\$53.64			
Continuing Value	\$1,012.92										
Monte Carlo Simulation Assumptions						Monte Carlo Simulation Results					
	Base	Stdev	Min	Max	Distribution			Intrinsic Value	1y-Target		
Revenue Variation	0	10%	N/A	N/A	Normal			Mean est.	\$34.29	\$38.89	
Op. Costs Variation	0	10%	N/A	N/A	Normal			σ(e)	\$0.22	\$0.26	
Country Risk Premium	6%	N/A	5%	7%	Triangular			3 σ(e) adjusted price	\$33.63	\$38.11	
Long term Growth	3%	N/A	3%	7%	Triangular			Current Price	\$28.75		
									Analysts' median est.	\$34.00	

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Knoll, Inc.	knl	Analyst Matthew Darcy	Current Price \$23.00	Intrinsic Value \$22.85	Target Value \$29.57	Divident Yield 2.04%	Target Return 1-y Return: 30.62%	BULLISH		
General Info		Peers		Market Cap.		Management				
Sector	Industrials	Herman Miller Inc.	\$1,713.33	Professional		Title				
Industry	Commercial Services and Supplies	HNI Corp.	\$2,282.44	Cogan, Andrew	Chief Executive Officer, Acting Pre	Comp. FY2012	Comp. FY2013	Comp. FY2014		
Last Guidance	Feb-04-2015	Steele Inc.	\$2,261.63	Spray, Craig	Chief Financial Officer, Chief Acct	\$3,143,093	\$2,752,000	\$10,975,254		
Next earnings date	7/20/2015	Kimball International, Inc.	\$408.51	Ahrens, Pamela	Senior Vice President of Sales & Di	\$0	\$2,271,183	\$657,800		
Market Data		Okamura Corp.	\$889.10	Pardo, Benjamin	Executive Vice President and Direc	\$921,910	\$783,200	\$957,550		
Enterprise value	\$1,411.77	Current Capital Structure		Beattie, Michael	Global Chief Information Officer	\$0	\$0	\$808,619		
Market Capitalization	\$1,126.45	Total debt/market cap	26.63%	Pollner, Michael	Senior Vice President, General Cou	\$0	\$0	\$0		
Daily volume	0.31	Cost of Borrowing	2.83%	Historical Median Performance						
Shares outstanding	48.98	Interest Coverage								
Diluted shares outstanding	48.16	Altman Z								
% shares held by institutions	97.46%	Debt Rating	BBB							
% shares held by insiders	3.95%	Levered Beta	0.92							
Short interest	2.12%	WACC (based on market value weights)	7.00%							
Days to cover short interest	2.96	Past Earning Surprises								
52 week high	\$24.42	Revenue	EBITDA	Norm. EPS						
52-week low	\$16.45	Last Quarter	0.0%	50.0%						
5y Beta	1.17	Last Quarter-1	0.8%	2.9%						
6-month volatility	25.70%	Last Quarter-2	3.3%	12.5%						
Proforma Assumptions		Last Quarter-3	5.2%	21.3%						
		Last Quarter-4	4.0%	13.2%						
Forecast		Valuation		Pricing Model						
		Period	Rev. Growth	Adj. Op. Cost/Rev	Invested Capital	NOPLAT Margin	ROIC	WACC		
		LTM	21.8%	88.7%	\$664.70	7%	8.5%	7.0%		
		NTM	8.6%	88.5%	\$651.93	8%	13.9%	7.0%		
		NTM+1	10.0%	88.4%	\$657.15	8%	15.1%	7.2%		
		NTM+2	3.3%	88.2%	\$663.76	8%	15.5%	7.4%		
		NTM+3	4.5%	88.0%	\$674.72	8%	16.1%	7.5%		
		NTM+4	4.5%	87.8%	\$686.80	8%	16.7%	7.7%		
		NTM+5	4.5%	87.7%	\$699.59	8%	17.4%	7.9%		
		NTM+6	4.5%	87.5%	\$714.36	8%	18.1%	8.1%		
		NTM+7	4.5%	87.3%	\$730.30	8%	18.8%	8.2%		
		NTM+8	4.5%	87.2%	\$745.20	8%	19.5%	8.4%		
		Continuing Period	4.5%	87.0%	\$345.97	7%	13.0%	8.5%		
		DCF (Weight = 100%)	Relative (Weight = 0%)	Distress (Weight = 0%)	Weighted Average Price Per Share					
		LTM	\$0.00	\$300.00	\$66.23	48.98	\$23.80	\$19.25	\$21.60	\$23.80
		NTM	\$45.82	\$300.00	-\$220.54	48.98	\$30.32	\$28.86	\$27.77	\$30.32
		NTM+1	\$51.52	\$300.00	-\$268.60	48.98	\$31.62	\$32.63	\$29.05	\$31.62
		NTM+2	\$53.29	\$300.00	-\$321.83	48.98	\$33.05	\$35.18	\$30.38	\$33.05
		NTM+3	\$56.90	\$300.00	-\$370.26	48.98	\$34.48	\$38.01	\$31.71	\$34.48
		NTM+4	\$60.91	\$300.00	-\$422.25	48.98	\$36.07	\$41.02	\$33.11	\$36.07
		NTM+5	\$65.39	\$300.00	-\$478.33	48.98	\$37.50	\$44.22	\$34.97	\$37.50
		NTM+6	\$70.29	\$300.00	-\$537.69	48.98	\$39.08	\$47.59	\$36.97	\$39.08
		NTM+7	\$75.46	\$300.00	-\$601.67	48.98	\$40.70	\$51.45	\$39.12	\$40.70
		NTM+8	\$81.03	\$300.00	-\$672.90	48.98	\$42.26	\$55.64	\$41.44	\$42.26
		Continuing Value	\$803.40							
Monte Carlo Simulation Assumptions		Monte Carlo Simulation Results								
		Base	Stdev	Min	Max	Distribution				
		Revenue Variation	0	10%	N/A	N/A	Normal	Mean est.	Intrinsic Value	1y-Target
		Op. Costs Variation	0	10%	N/A	N/A	Normal	σ(e)	\$23.80	\$30.32
		Country Risk Premium	6%	N/A	5%	7%	Triangular	3 σ(e) adjusted price	\$0.32	\$0.25
		Long term Growth	5%	N/A	3%	7%	Triangular	Current Price	\$22.84	\$29.57
								Analysts' median est.	\$23.00	\$27.50