March 2, 2018

Thor Industries: THO

David Blanco

Sector: Consumer Discretionary
Industry: Automobiles & Components
Current Price: $131.68
Target Price: $136.68

Company Description: Thor Industries manufactures recreational vehicles (RV) in Indiana, US and operates primarily throughout the United States and Canada. The company's product line include towable vehicles and motorized recreational vehicles. Thor industries is currently the largest RV manufacturer in the US.

SELL

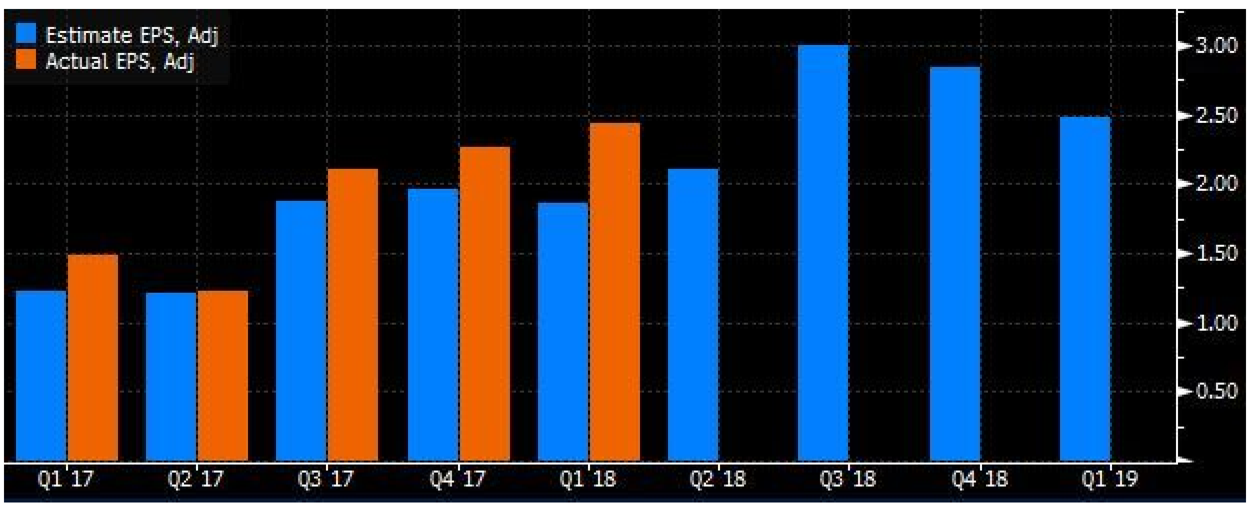
Current Price: $121.11
Target Price: $136.68
Market Cap: 6.3B
Beta: 1.32
Average Volume: 595,577
ROE: 26.34%
Cost of Equity: 9.1%
Debt-to-Equity: 1%

Thesis: Thor has grown exponentially as the booming economy overwhelmingly benefits the recreational vehicle market. Low interest rates, large credit availability, and high consumer confidence allowed Thor to expand its operations. However, dropping prices reflect the decreasing analysts' faith that Thor will continue to expand as quickly as it has for the past eight years. Interest hikes and increased expected inflation would hit this market especially harshly, which indicates that Thor Industries will be deemed overpriced once the economy begins to show signs of overheating.

Catalysts:

- **Short Term(within the year):** Thor enjoyed exponential growth and lower expenses as a percentage of revenue due to the acquisition of Jayco in the first month of 2017. Thor announced this would result in lower revenue growth in the latter half of 2018 as Jayco's integration is completed.
- **Mid Term(1-2 years):** Economic data suggests that rising inflation as well as wage increases are becoming prevalent as the labor market tightens. If this trend continues, Thor will face a lower operating margin.
- **Long Term(3+):** Thor's aggressive growth for the ninth consecutive year faces various obstacles. As the Fed prepares to initiate a series of interest hikes, the RV market will be heavily impacted as it thrived due to the government's expansionary policy that fomented consumer spending. This new policy will most likely result in slower growth for the RV market, which has been the justification for Thor's explosive stock price growth.

Earnings Performance:



Thor's meteoric rise in its price valuation versus the consumer discretionary index is no surprise once earnings performance are considered. since 2016, Thor industries has consistently beaten analysts' estimates. Several factors have allowed Thor to surprise estimates. Some have been out of their control, such as rising demand for RV, while others have been strategic decisions. Thor has thrived due to various acquisitions it has made in the past decade to grow its revenue and income. Those include the purchase of K-Z Inc (towable vehicle manufacturer), Postle Aluminum Co. (aluminum manufacturer), and Cruiser RV (RV manufacturer). These acquisitions have allowed Thor industries to grow YoY in the double digits in terms of revenue without compromising costs, proven by the uptick in EPS growth.

Jayco Acquisition:

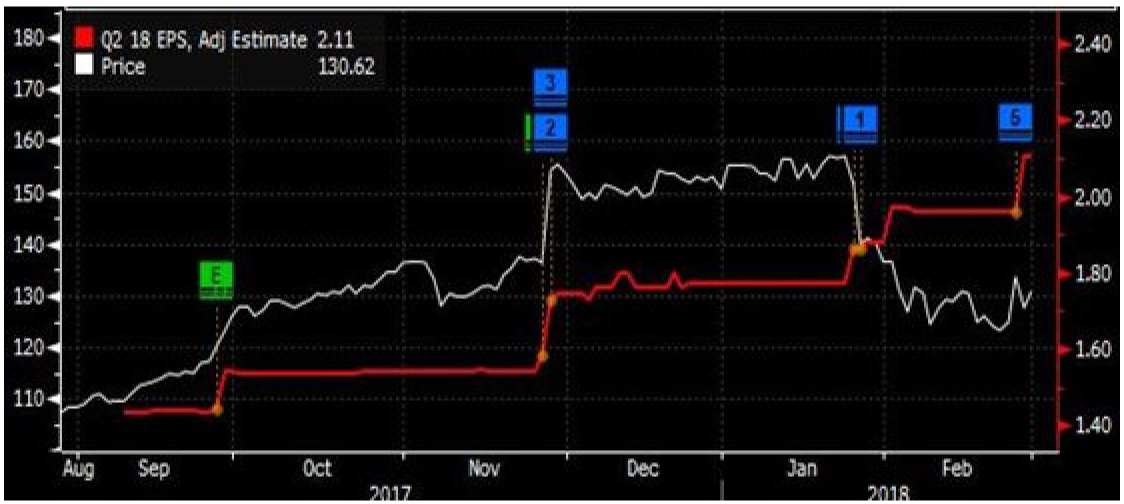
Among these acquisitions that have significantly increased the market share of Thor, the most significant has been Jayco Corp. Jayco is the number one selling travel trailer that also operates in Indiana and parts of Idaho. This acquisition was finalized in June 30, 2016 on a Stock Purchase Agreement for a cash consideration of $562,690,000. This purchase increased the overall offering of towable and motorized RVs in addition to expanding into the high-end Class A and Class C motorhomes. Jayco's acquisition accounted for 39.6% of the 58.2% increase in revenue in 2017. This acquisition was exceptionally beneficial for Thor, which not only saw a significant increase in revenue but also succeeded in reducing operating expenses as a percentage of revenue that increased gross profit and EBITDA.

In Millions of USD	2014 Y	2015 Y	2016 Y	2017 Y	Current/LTM	2018 Y Est	2019 Y Est
12 Months Ending	07/31/2014	07/31/2015	07/31/2016	07/31/2017	10/31/2017	07/31/2018	07/31/2019
Revenue, Adj	3,525.5	4,006.8	4,582.1	7,247.0	7,770.1	8,572.4	9,117.4
Growth %, YoY	8.8	13.7	14.4	58.2	47.7	18.3	6.4
Gross Profit, Adj	471.2	557.5	726.3	1,043.6	1,140.0	1,274.1	1,304.8
Margin %	13.4	13.9	15.9	14.4	14.7	14.9	14.3
EBITDA, Adj	275.4	322.0	444.6	655.8	721.8	820.4	903.4
Margin %	7.8	8.0	9.7	9.0	9.3	9.6	9.9
Net Income, Adj	176.5	202.0	263.8	372.8	422.9	496.7	552.7
Margin %	5.0	5.0	5.8	5.1	5.4	5.8	6.1
EPS, Adj	3.31	3.80	5.02	7.06	8.01	10.78	11.59
Growth %, YoY	9.3	14.9	32.1	40.7	45.4	52.6	7.5

2017 already shows the radical increase in revenue and EPS growth. The 2018 and 2019 estimates already predict that if nothing changes, Thor could be looking at YoY EPS percentage growth of 52.6% and 7.5%, respectively. The drop in growth is due to the realization of Jayco's integration at the end of 2018.

January Drop:

Thor became popular start (in terms of volume traded) starting 2016 due to the company's apparent ability to consistently beat analysts' estimates. As analysts continued to increase their EPS estimates, price's growth followed them closely, always slightly higher as stockholders had confidence in Thor. As revenue and net income margins showed before, these were no unjustified price hikes, as the company continued to expand its operations and increase its profitability. With the Trump administration coming in at the beginning of 2017, the company's stock price climbed even higher due to the promise of tax cuts, higher consumer confidence (PMI increased from 56.3 to 59.8 during 2017), and deregulation of the coal industry. As a company highly dependent on macroeconomic factors, the expected increase in consumer spending increased even more Thor's prices. However, at the end of January, 2018, something unexpected happened.



For the first time, prices began to drop significantly, falling below EPS estimates. From a PE perspective, this was a great moment. Analysts began writing regarding Thor's "cheap" stock and how it was bound to rise given the continued increasing expected return from growing revenue. However, once you look at the factors that began this drop in prices, the reason why prices fell becomes more grim. In February 28, analysts downgraded Thor's stock from a buy to a hold. The reason why is obvious once you consider how it continued dropping after the January jobs report. The US labor market has finally begun tightening and inflation is on the rise. While the S&P 500 managed to recover after a tumultuous weekend, Thor continues to drop. Thor outperformed the market significantly not only from its acquisitions, but because the consumption increase especially benefited the RV market. Now that inflation has begun to set in, it might not only result in higher wage costs for Thor, but it makes uncertain how much growth Thor will experience from now on. Thor's price continued to climb due to the consensus that the RV market would continue to ride the wave of the bullish market. However, after the markets recovered from the January ordeal, stockholders are no longer so confident that Thor will undoubtedly continue to expand at the rate it has. In a way, it could be said that Thor's risk premium has increased, as the market's ever-rising expectation has begun waning.

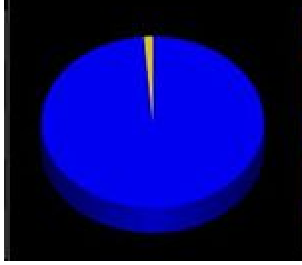
	Name (BICS Best Fit)	Mkt Cap (USD)	Last Px	Chg Pct 1D	Chg Pct 1M	Rev - 1 Yr Gr:Y	EPS - 1 Yr Gr:Y	P/E	ROE	Dvd 12M Yld
	Median	2.09B	53.19	1.14%	-1.31%	24.72%	35.99%	18.60	24.29%	1.39%
100)	THOR INDUSTRIES INC	6.90B	130.85	2.68%	-4.25%	58.16%	40.70%	16.33	28.10%	1.07%
101)	WINNEBAGO INDUSTRIES	1.40B	44.35	1.96%	-2.42%	58.64%	35.40%	17.87	18.42%	0.90%
102)	MARINE PRODUCTS CORP	506.69M	14.57	-0.14%	-0.21%	10.77%	35.99%	24.07	31.07%	2.47%
103)	JOHNSON OUTDOORS INC-A	619.94M	62.02	0.30%	2.91%	13.10%	76.64%	16.48	16.74%	0.61%
104)	LCI INDUSTRIES	2.78B	111.35	0.32%	1.00%	27.93%	10.77%	19.34	24.29%	1.84%
105)	CAMPING WORLD HOLDIN...	4.14B	43.31	4.87%	-3.22%	21.51%	--	223.98	--	1.72%

This does not mean Thor is a bad company, quite the contrary. Thor outperforms its competitors (the biggest being Winnebago industries) on almost any metric. Above it is shown how Thor is superior in terms of EPS growth, ROE and dividend yield. The argument, however, is not that Thor is a bad company, but an overpriced stock due to the risk factors to be considered. Thor's executives themselves believe that the biggest factors to their success are the macroeconomic ones such as "industry demand,retail patterns, dealer confidence, and economic condition." While the economy is not really expected to fall into a recession, the possibility has certainly begun appearing, and since it would affect the RV market especially hard. To achieve a fair valuation (which is to recover back to $150.64, its December value, within a year), the company is expected to grow revenue-wise at 15% while maintaining its current risk-premium. However, given the current volatility of the market, the previously-calculated equity premium is lower than it should be, and that is why once that is considered in the calculations, its current $120 price range is justified.

Interest Hikes: (no debt though-consumer spending, buyback dealer deal, credit crunch) Debt,

If the market's current valuation is appropriate, why not simply hold the stock? The issue to consider then are the non-systemic risk that Thor faces versus its competitors. The last factor to consider with the current economy is interest. As it stands, interest rates are expected to rise with new Fed's policies. How exposed is Thor Industries to a possible credit crunch? Currently, Thor could be said to be wholly unaffected if interest rates increase. While Thor Industries has a $500M credit facility on a three-year renewal basis, it currently holds virtually no debt.

Capital Structure (Millions of USD)



Market Cap	7,178.0	98.8%
ST Debt	0.0	0.0%
LT Debt	90.0	1.2%
Pref. Eqty	0.0	0.0%
Total	7,268.0	100.0%

While companies that have loaded themselves on cheap debt might face possible destabilizing futures once interest hikes kick in, Thor will not be affected in such a way. However, Thor might suffer in another fashion: M&A. Thor has been able to grow in the past century due to its strategic acquisitions, which have been partially financed through debt, the primary function of the credit facility. If interest rates were to rise significantly Thor would not be able to benefit as it has from its aggressive acquisition strategy.

Dealers:

While an acquisition stop may hinder growth, the real issue with interest hikes and a tightening of credit has to do with Thor Industries' dealers. Thor does not finance its dealers, but rather dealers finance themselves through a "floor plan" with an unaffiliated bank. As such, dealers are able to finance themselves provided that Thor Industries promises to repurchase the products if dealers are unable to sell them within 18 months. This is especially troubling once you consider that ¾ of Thor's total assets are inventory and accounts receivable.

As interest rates continue to rise, dealers will most likely lower their purchasing orders, reducing overall revenue. However, if consumption were to fall even by 1%, Thor could potentially be facing not only reduced revenue, but an obligation to buy back its sold products, as dealers find it hard to sell Thor's products. With that in mind, a volatile market should definitely increase the risk premium for Thor. Their inventory and accounts payable might as well be unearned revenue, as they recognize when they sell it to a dealer, not when the dealer manages to sell it himself. This is why a slight contraction in consumption would be bad for the overall market, but devastating for Thor. As it stands, Thor takes up all the risk associated with the sale of its products while banks and dealers make a profit and hold no risk whatsoever. While its ROE is high and reflects the true return as a whole, it hides the fact that it faces as much risk as a company ridden with debt on an economy with rising interest rates.

Conclusion:

Thor is a thriving company in a growing industry where it holds a high market share. The company has successfully justified its increase in price in the past two years given its substantial growth in revenue, operating margin, and EPS and beaten all estimates. However, the drop in price in the past two months is not only a result of fear of a market of possible inflation, but the market's realization of Thor's inherent risk. The market has adjusted its price due to the volatility of Thor's expected growth given the uncertainty in the market and the risk factors associated with Thor's current sales' tactics. Just as Thor's stock has benefitted from its market's growing demand, even a small slowdown could result in terrible net income for the company in addition to the revenue loss. With those factors taken into consideration to the company's valuation, this company should be replaced with a company with substantially less unsystematic risk that is not compensated for.

CENTER FOR GLOBAL FINANCIAL STUDIES

Thor Industries, Inc. (tho) — **NEUTRAL**

Analysis by thor industries	Current Price:	$126.04	Intrinsic Value	$39.64	Target 1 year Return: 9.44%
2/28/2018	Divident Yield:	1.2%	Target Price	$136.46	Probability of Price Increase: 0%

Description

Thor Industries, Inc., through its subsidiaries, designs, manufactures, and sells recreational vehicles, and related parts and accessories primarily in the United States and Canada.

General Information

Sector	Consumer Discretionary
Industry	Automobiles
Last Guidance	February 12, 2018
Next earnings date	March 7, 2018

Market Assumptions

Estimated Equity Risk Premium	5.09%
Effective Tax rate	21%

Market Data

Market Capitalization	$6,634.22
Daily volume (mil)	0.23
Shares outstanding (mil)	52.69
Diluted shares outstanding (mil)	52.79
% shares held by institutions	109%
% shares held by investments Managers	72%
% shares held by hedge funds	8%
% shares held by insiders	4.12%
Short interest	4.93%
Days to cover short interest	3.61
52 week high	$161.48
52-week low	$87.96
Volatility	24.61%

Past Earning Surprises

Quarter ending	Revenue	EBITDA
10/31/2016	13.83%	21.67%
1/31/2017	5.10%	2.35%
4/30/2017	3.49%	14.75%
7/31/2017	4.07%	16.52%
10/31/2017	12.89%	31.12%
Mean	7.88%	17.28%
Standard error	1.0%	3.9%

Market and Credit Scores

Recommendation (STARS) Value--0
Recommendation (STARS) Description--0
Quality Ranking Value--B+
Quality Ranking Description--Average
Short Score--1
Market Signal Probability of Default % (Non-Ratings)--0.979%
CreditModel Score (Non-Ratings)--bbb+

Industry and Segment Information

LTM Revenues by Geographic Segme	LTM Revenues by Business Segments
United States--91%	Recreation Vehicles - Towables--71%
Canada--9%	Recreation Vehicles - Motorized--27%
--	Other--3%
--	Intercompany Eliminations---1%
--	--

Peers

Winnebago Industries, Inc.	--
Polaris Industries Inc.	--
Brunswick Corporation	--
--	--
--	--

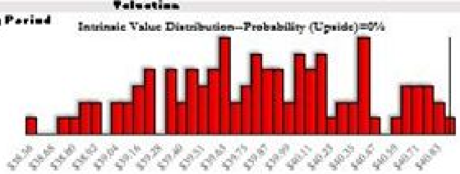
Management	Position	Total Compensations Growth	Stock Price Growth During Tenure
Orthwein, Peter	Co-Founder & Executive Chairman	2.26% per annum over 6y	11.67% per annum over 6y
Martin, Robert	CEO, President & Director	22.96% per annum over 6y	11.67% per annum over 6y
Zuhl, Colleen	CFO & Senior VP	39.05% per annum over 5y	1.74% per annum over 5y
Julian, Kenneth	Senior Vice President of Administration & Hum	27.23% per annum over 4y	7.32% per annum over 4y
Woelfer, W.	Senior VP, General Counsel & Corporate Secre	25.2% per annum over 5y	1.74% per annum over 5y
Byatt, Bruce	Senior Director of Investor Relations		

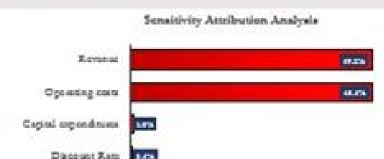
Profitability	tho (LTM)	tho Historical	Peers' Median (LTM)
Return on Capital (GAAP)	24.7%	23.35%	16.43%
Operating Margin	6%	5.47%	9.00%
Revenues/Capital (GAAP)	4.22	4.27	1.83
ROE (GAAP)	37.7%	27.2%	15.7%
Net margin	6.5%	6.1%	4.3%
Revenues/Book Value (GAAP)	5.80	4.43	3.68
Invested Funds	**tho (LTM)**	**tho Historical**	**Peers' Median (LTM)**
Cash/Capital	11.4%	20.8%	15.8%
NWC/Capital	12.1%	14.2%	12.1%
Operating Assets/Capital	55.3%	38.9%	43.1%
Goodwill/Capital	21.2%	26.0%	29.1%
Capital Structure	**tho (LTM)**	**tho Historical**	**Peers' Median (LTM)**
Total Debt/Market Capitalization	0.06	0.06	0.43
Cost of Debt	4.0%	4.0%	5.2%
CGFS Rating (F-score, Z-score, and default Probabilit	AA		
WACC	8.0%	8.9%	10.0%

Porter's 5 forces (Scores are percentiles)

Valuation

Forecast Assumptions	Explicit Period (8 years)	Continuing Period
Revenue Growth CAGR	4%	2%
Average Operating Margin	6%	7%
Average Net Margin	4%	4%
Growth in Capital CAGR	11%	2%
Growth in Claims CAGR	9%	2%
Average Return on Capital	10%	6%
Average Return on Equity	12%	6%
Average Cost of Capital	8%	8%
Average Cost of Equity Ke	8%	8%





Below, insert a screenshot of your “OUTPUT” page from the Pro-Forma. Or, if you built your own model, insert screenshot of it here.