

Patrick Industries, Inc.

Worsening end market outlook to offset solid execution; Reiterate Underperform

Reiterate Rating: UNDERPERFORM | PO: 63.00 USD | Price: 66.17 USD

Reiterate Underperform on end market headwinds

We reiterate our Underperform on Patrick despite its recent solid execution given a worsening outlook for its key end markets (RV, marine and housing). On its February 9 earnings call, PATK management forecasted recreational vehicle (RV) (53% of 2022 sales) wholesale unit shipments of 325K to 350K (down 30-35% YoY) and retail shipments of 360K to 380K (down 15-20% YoY). We believe management's retail expectation (which is in-line with the average over the last decade) will prove optimistic and demand will remain soft through 2H23 given: 1) higher carrying costs and tighter credit will cause dealers to destock inventory below historical levels, 2) higher rates and tighter credit will also pressure consumer demand for RVs, and 3) we believe some RV demand was pulled forward into 2020/2021 during the pandemic. In marine (21% of 2022 revenue), sales should be relatively resilient given lean channel inventory, but end market demand will likely soften in a more challenging macro environment. We expect the industrial segment (10%+ of sales) to decline in 2023 on slowing housing starts.

Margins declining from peak levels, but resetting higher

Management expects 2023 operating margin in the 7.5%-8.0% range in 2023 (vs. our 7.9% est), down from 10.2% in 2022. Despite the YoY decline, operating margin will remain above pre-COVID levels given favorable M&A mix shift (higher marine mix) and automation benefits. We estimate efficiency gains have driven 100-125bps of the margin improvement. In addition, PATK's expense base is highly variable (83% of workforce is hourly) and the company has already taken steps to right size production. We estimate PATK has raised prices on RV components by roughly 30% since 2020 as the company passed along higher input costs including labor, freight and materials. We anticipate PATK to pass some of the savings from commodity deflation to customers.

Raise PO to \$63, but reiterate Underperform

We lower our 2023/2024 EPS forecasts by roughly 8%/18% to reflect the weaker macro backdrop, slowing end market demand especially in RV and housing and RV dealer destocking. We raise our PO to \$63 (from \$53), as we roll our multiple forward to 2024 and use a higher multiple on more conservative estimates (now based on 5.5x 2024E EV/EBITDA multiple vs. previous 5x 2023E EV/EBITDA multiple). While PATK's valuation already reflects a bearish scenario, we do not see a near-term catalyst for re-rating and we are modeling 2023/2024 EPS 9%/18% below consensus.

Estimates (Dec) (US\$)	2021A	2022A	2023E	2024E	2025E
EPS	9.63	13.48	7.06	7.45	8.53
GAAP EPS	9.63	13.41	7.06	7.45	8.53
EPS Change (YoY)	129.3%	40.0%	-47.6%	5.5%	14.5%
Consensus EPS (Bloomberg)			7.59	9.07	NA
DPS	1.17	1.32	1.34	1.36	1.38
Valuation (Dec)					
P/E	6.9x	4.9x	9.4x	8.9x	7.8x
GAAP P/E	6.9x	4.9x	9.4x	8.9x	7.8x
Dividend Yield	1.8%	2.0%	0%	0%	2.1%
EV / EBITDA*	5.7x	4.2x	6.7x	6.5x	6.0x
Free Cash Flow Yield*	12.9%	22.8%	32.6%	10.8%	12.7%

* For full definitions of *IQmethod*SM measures, see page 8.

27 March 2023

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	53.00	63.00
2023E EPS	8.21	7.06
2024E EPS	10.53	7.45
2025E EPS	NA	8.53

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Stock Data

Price	66.17 USD
Price Objective	63.00 USD
Date Established	27-Mar-2023
Investment Opinion	C-3-7
52-Week Range	41.75 USD - 77.96 USD
Mrkt Val (mn) / Shares Out (mn)	1,456 USD / 22.0
Average Daily Value (mn)	11.45 USD
BofA Ticker / Exchange	PATK / NAS
Bloomberg / Reuters	PATK US / PATK.OQ
ROE (2023E)	15.4%
Net Dbt to Eqty (Dec-2022A)	132.0%

ESGMeter™ **Low**

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to ["BofA ESGMeter Methodology"](#).

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Refer to important disclosures on page 9 to 11. Analyst Certification on page 7. Price Objective Basis/Risk on page 7.

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Timestamp: 27 March 2023 05:11AM EDT

iQprofileSM Patrick Industries, Inc.

iQmethodSM – Bus Performance*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Return on Capital Employed	16.3%	18.0%	9.3%	9.1%	9.5%
Return on Equity	33.9%	38.3%	15.4%	14.1%	14.3%
Operating Margin	8.6%	10.2%	7.9%	7.8%	8.4%
Free Cash Flow	187	332	474	157	185

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash Realization Ratio	1.1x	1.2x	3.6x	1.6x	1.6x
Asset Replacement Ratio	1.2x	1.1x	1.3x	1.4x	1.3x
Tax Rate	23.5%	24.6%	25.5%	25.5%	25.5%
Net Debt-to-Equity Ratio	151.6%	132.0%	86.1%	66.2%	47.5%
Interest Cover	6.9x	9.1x	4.5x	4.6x	5.0x

Income Statement Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Sales	4,078	4,882	3,558	3,704	3,852
% Change	64.0%	19.7%	-27.1%	4.1%	4.0%
Gross Profit	801	1,060	783	807	847
% Change	NA	NA	NA	NA	NA
EBITDA	457	627	391	402	437
% Change	85.1%	37.3%	-37.7%	3.0%	8.7%
Net Interest & Other Income	(58)	(61)	(70)	(70)	(70)
Net Income (Adjusted)	225	330	157	164	188
% Change	131.7%	45.9%	-52.0%	4.1%	14.5%

Free Cash Flow Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Income from Cont Operations (GAAP)	225	328	158	164	188
Depreciation & Amortization	56	73	78	81	85
Change in Working Capital	(110)	(61)	299	(17)	(16)
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	81	71	39	39	39
Capital Expenditure	(65)	(80)	(100)	(110)	(110)
Free Cash Flow	187	332	474	157	185
% Change	NA	NA	NA	NA	NA

Balance Sheet Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash & Equivalents	123	23	346	470	623
Trade Receivables	172	173	146	152	158
Other Current Assets	679	714	473	492	509
Property, Plant & Equipment	319	351	342	339	334
Other Non-Current Assets	1,357	1,522	1,642	1,642	1,642
Total Assets	2,651	2,782	2,949	3,096	3,266
Short-Term Debt	8	8	8	8	8
Other Current Liabilities	425	360	392	399	406
Long-Term Debt	1,279	1,276	1,276	1,276	1,276
Other Non-Current Liabilities	171	184	184	184	184
Total Liabilities	1,883	1,827	1,859	1,867	1,874
Total Equity	768	955	1,090	1,229	1,392
Total Equity & Liabilities	2,651	2,782	2,949	3,096	3,266

* For full definitions of iQmethodSM measures, see page 8.

Company Sector

Building Products

Company Description

PATK is a leading component and building products supplier to the RV (59% of sales), marine (16% of sales), manufactured housing (14%) and industrial (11%) end markets. PATK successfully diversified its business away from RVs and expanded its geographic presence through M&A. These acquisitions, along with solid pricing power and market share gains, have led to increased content per unit across segments. Patrick Industries was founded in 1959 and is headquartered in Elkhart, Indiana.

Investment Rationale

We rate PATK shares at Underperform. Patrick is well positioned within the RV and marine markets, however, we see a challenging outlook for PATK shares and end markets in a rising rate environment.

Stock Data

Average Daily Volume

173,006

Quarterly Earnings Estimates

	2022	2023
Q1	4.54A	1.77E
Q2	4.79A	2.12E
Q3	2.43A	1.71E
Q4	1.68A	1.46E

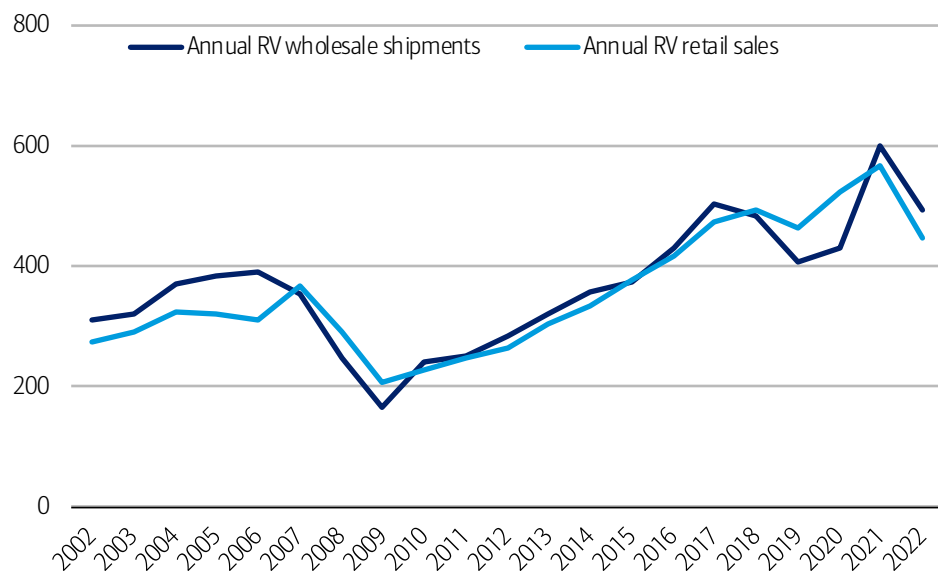
Reiterate Underperform on end market headwinds

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- Retail shipments for recreational vehicles (RV) declined roughly (21%) YoY in 2022 and wholesale shipments declined 18% YoY. THOR industries/customer commentary suggests destocking will continue through 1H23 and into 2H23.

Exhibit 1: RV wholesale shipments and retail units (units, 000s)

RV wholesale shipments have outpaced retail sales over the last two years



Source: BofA Global Research, RVIA

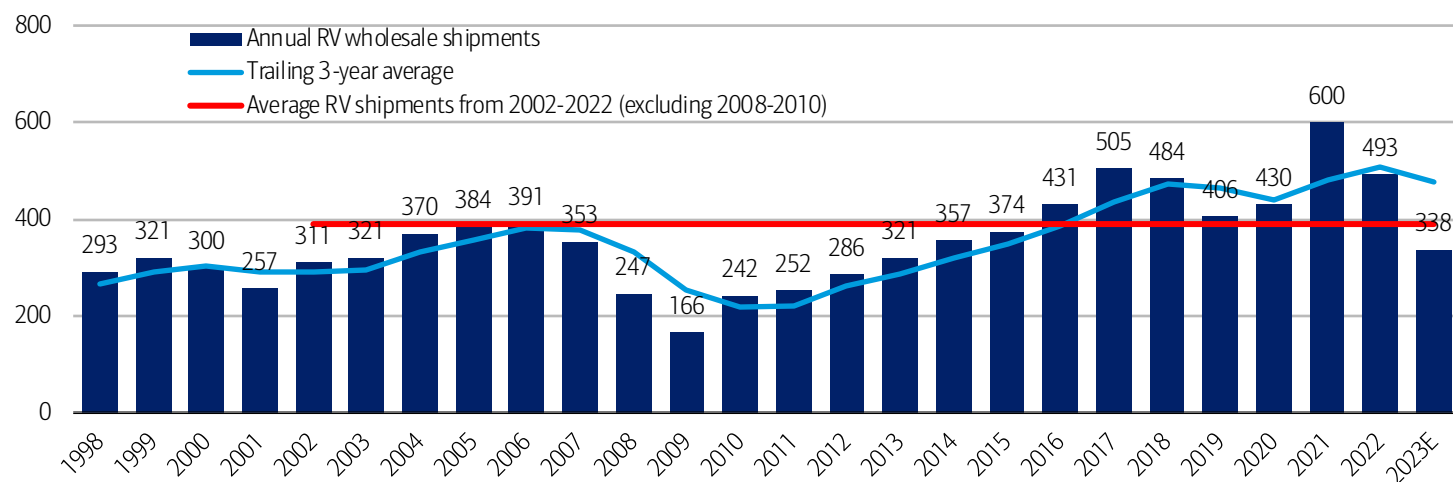
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- We believe some demand was pulled forward into 2020/2021 during the pandemic, which could pressure retail sales in 2023 and 2024.



Exhibit 2: Annual wholesale RV shipments (including PATK 2023 estimate)

Shipments averaged 360K from 2000-2022



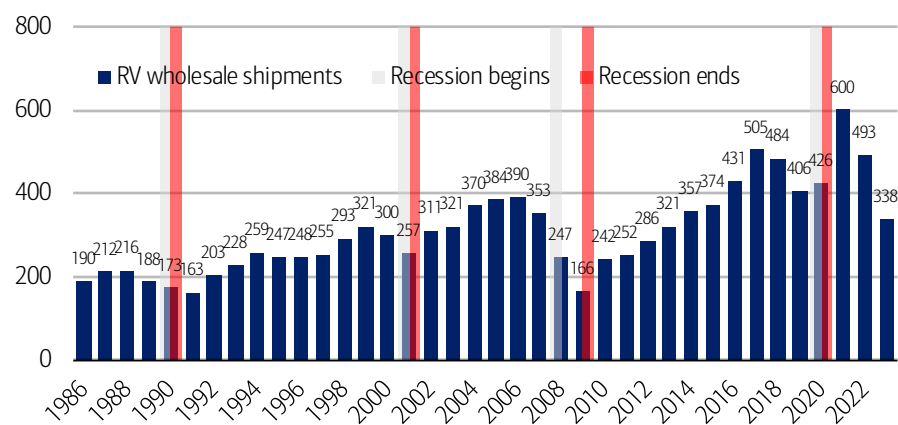
Source: BofA Global Research, RVIA

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- Weakening macro outlook (potential recession) would likely weigh on RV demand.

Exhibit 3: Annual wholesale RV shipments during recessions

RV sales typically decline meaningfully before and during recessions... and recover quickly in following years



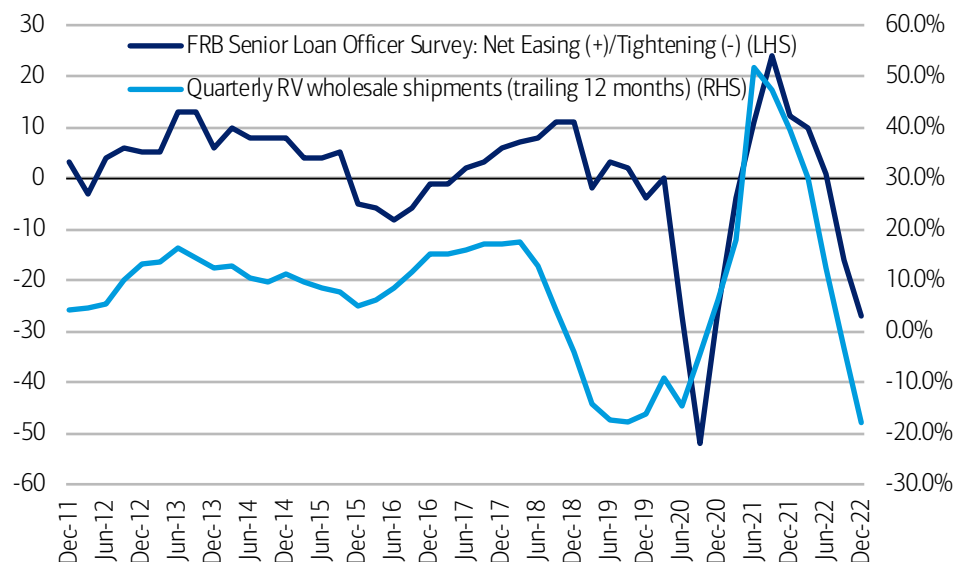
Source: BofA Global Research, RVIA

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- Tighter credit standards could also pressure demand in large ticket discretionary items like RVs and marine.

Exhibit 4: Tighter lending standards could pressure RV sales

Fed's Senior Loan Officer Opinion Survey (SLOOS) shows lending standards are tightening



Source: BofA Global Research, FRB Senior Loan Officer Survey; RMA

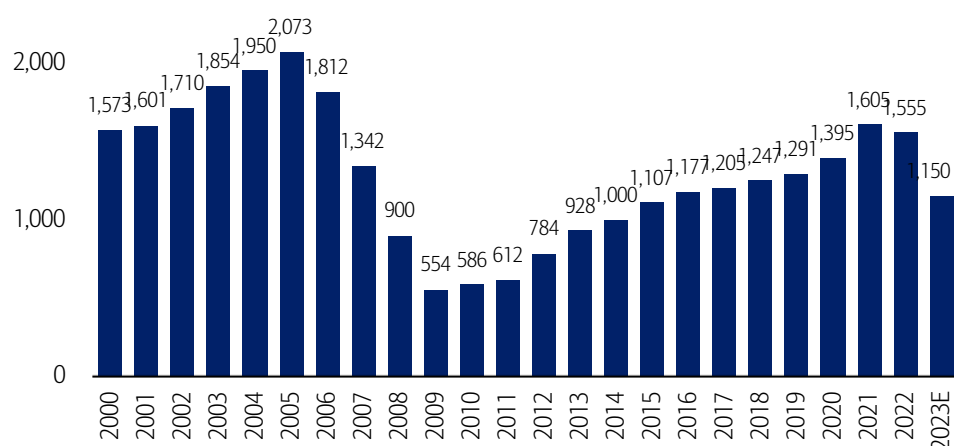
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- Marine (21% of 2022 revenue): Wholesale marine shipments are expected to be down low-double digits and retail down low single digits in 2023.
- Housing: We expect the industrial (11% of 2022 revenue) segment to decline in 2023 on slowing housing starts and manufactured housing (15% of 2022 revenue) to also decline given macro headwinds.

Exhibit 5: US total home starts (thousand units)

Starts averaged ~1.3M from 2000-2022

3,000



Source: US Census Bureau, BofA global research estimates

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Exhibit 7: Patrick Industries income statement (\$ millions, except per share data)

We expect earnings to moderate in 2023

YE 12/31	2023E				2022	2023E	2024E
	3/31/2023	6/30/2023	9/30/2023	12/31/2023	12/31/2022	12/31/2023	12/31/2024
	1QE	2QE	3QE	4QE			
Net Sales	\$912.9	\$961.0	\$845.3	\$839.2	\$4,881.9	\$3,558.3	\$3,703.7
Cost of goods sold	712.1	749.6	659.3	654.5	3,821.9	2,775.5	2,896.3
Gross Profit	\$200.8	\$211.4	\$186.0	\$184.6	\$1,059.9	\$782.8	\$807.4
Warehouse & delivery	36.5	38.4	33.8	33.6	163.0	142.3	148.1
Selling, general & administrative	73.0	73.0	64.2	70.5	327.5	280.8	287.8
Amortization of intangible assets	19.3	19.5	19.7	19.9	73.2	78.2	81.4
Operating income	\$72.0	\$80.5	\$68.3	\$60.7	\$496.2	\$281.5	\$290.1
Interest expense	17.5	17.5	17.5	17.5	60.8	70.0	70.0
Earnings before income taxes	\$54.5	\$63.0	\$50.8	\$43.2	\$435.4	\$211.5	\$220.1
Income tax expense	13.9	16.1	12.9	11.0	107.2	53.9	56.1
Earnings from continuing operations	\$40.6	\$46.9	\$37.8	\$32.2	\$328.2	\$157.6	\$164.0
Net income attributable to PATK	\$40.6	\$46.9	\$37.8	\$32.2	\$328.2	\$157.6	\$164.0
Non-recurring items	-	-	-	-	-	-	-
GAAP Net Income	\$40.6	\$46.9	\$37.8	\$32.2	\$330.0	\$157.6	\$164.0
Diluted EPS (GAAP, less discontinued ops.)	\$1.77	\$2.12	\$1.71	\$1.46	\$13.48	\$7.06	\$7.45
Diluted EPS (Cont. Ops.)	\$1.77	\$2.12	\$1.71	\$1.46	\$13.48	\$7.06	\$7.45
Common Shares Outstanding:							
Diluted	22.9	22.1	22.1	22.1	24.5	22.3	22.0
EBITDA Calculation							
Adjusted Operating Profit	\$72.0	\$80.5	\$68.3	\$60.7	\$496.2	\$281.5	\$290.1
(+) other expense (income), net	-	-	-	-	-	-	-
(=) Adjusted EBIT	\$72.0	\$80.5	\$68.3	\$60.7	\$496.2	\$281.5	\$290.1
(+) Depreciation & Amortization	27.0	27.2	27.4	27.6	130.8	109.0	112.2
(=) Adjusted EBITDA	\$99.0	\$107.6	\$95.6	\$88.3	\$626.9	\$390.5	\$402.3
Margins							
Gross Margin	22.0%	22.0%	22.0%	22.0%	21.7%	22.0%	21.8%
Warehouse & Delivery % of Sales	4.0%	4.0%	4.0%	4.0%	3.3%	4.0%	4.0%
SG&A % Sales	8.0%	7.6%	7.6%	8.4%	6.7%	7.9%	7.8%
Operating Margin	7.9%	8.4%	8.1%	7.2%	10.2%	7.9%	7.8%
Adjusted EBIT Margin	7.9%	8.4%	8.1%	7.2%	10.2%	7.9%	7.8%
Adjusted EBITDA Margin	10.8%	11.2%	11.3%	10.5%	12.8%	11.0%	10.9%
Incremental EBITDA margin	21.7%	19.3%	11.4%	12.3%	21.2%	17.9%	8.1%
Pre-tax Margin	6.0%	6.6%	6.0%	5.1%	8.9%	5.9%	5.9%
Net Income (continuing ops)	4.5%	4.9%	4.5%	3.8%	6.7%	4.4%	4.4%
Tax rate	25.5%	25.5%	25.5%	25.5%	24.6%	25.5%	25.5%
YoY % Change							
Sales	(32.0%)	(34.9%)	(24.0%)	(11.8%)	19.7%	(27.1%)	4.1%
Gross Profit	(32.0%)	(35.4%)	(21.4%)	(8.2%)	32.3%	(26.1%)	3.1%
Operating Profit	(55.5%)	(53.7%)	(26.4%)	(10.2%)	41.1%	(43.3%)	3.1%
EBIT	(55.5%)	(53.7%)	(26.4%)	(10.2%)	41.1%	(43.3%)	3.1%
EBITDA	(48.4%)	(47.9%)	(24.1%)	(13.6%)	37.3%	(37.7%)	3.0%
Pre-tax Profit	(62.9%)	(60.4%)	(34.5%)	(16.7%)	48.2%	(51.4%)	4.1%
Net Income (continuing ops)	(63.9%)	(59.7%)	(35.7%)	(19.9%)	45.9%	(52.0%)	4.1%
EPS	(60.9%)	(55.6%)	(29.6%)	(13.4%)	40.0%	(47.6%)	5.5%

Source: BofA Global Research estimates, Company Data

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Price objective basis & risk

Patrick Industries, Inc. (PATK)

Our \$63 price objective is based on 5.5x 2023E adjusted EV/EBITDA, near the low-end Patrick's trading range over the last five years due to macro/demand concerns. Patrick is well positioned within the RV and marine markets, however, we see a challenging outlook for PATK shares and end markets in a rising rate environment..

Downside risks: 1) a weaker macroeconomic environment 2) deterioration in consumer confidence, 3) a rise in interest rates, 4) general weakness in RV and/or marine demand 5) a housing-related slowdown, 6) Customer concentration, 7) higher labor and raw material costs, and 8) acquisitions could fail to materialize or be dilutive.

Upside risks: 1) a stronger macroeconomic environment 2) lower interest rates, 3) strength in RV and/or marine demand 4) housing acceleration 5) lower labor and raw material costs.

Analyst Certification

I, Rafe Jadrosich, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Homebuilders and Building Products Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Armstrong World Industries, Inc.	AWI	AWI US	Rafe Jadrosich
	D.R. Horton, Inc.	DHI	DHI US	Rafe Jadrosich
	Latham Group, Inc.	SWIM	SWIM US	Shaun Calnan, CFA
	NVR, Inc.	NVR	NVR US	Rafe Jadrosich
	Owens Corning	OC	OC US	Rafe Jadrosich
	PulteGroup Inc.	PHM	PHM US	Rafe Jadrosich
	Toll Brothers, Inc.	TOL	TOL US	Rafe Jadrosich
NEUTRAL				
	Dream Finders Homes, Inc.	DFH	DFH US	Rafe Jadrosich
	KB Home	KBH	KBH US	Rafe Jadrosich
	Lennar Corporation	LEN	LEN US	Rafe Jadrosich
	The AZEK Company Inc.	AZEK	AZEK US	Rafe Jadrosich
UNDERPERFORM				
	Fortune Brands Innovations Inc	FBIN	FBIN US	Rafe Jadrosich
	Hayward Holdings, Inc.	HAYW	HAYW US	Rafe Jadrosich
	Masco Corp	MAS	MAS US	Rafe Jadrosich
	Mohawk Industries	MHK	MHK US	Rafe Jadrosich
	Patrick Industries, Inc.	PATK	PATK US	Rafe Jadrosich
	Pool Corporation	POOL	POOL US	Shaun Calnan, CFA
	Trex Company, Inc.	TREX	TREX US	Rafe Jadrosich



IQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity
Operating Margin
Earnings Growth
Free Cash Flow

Quality of Earnings

Cash Realization Ratio
Asset Replacement Ratio
Tax Rate
Net Debt-To-Equity Ratio
Interest Cover

Valuation Toolkit

Price / Earnings Ratio
Price / Book Value
Dividend Yield
Free Cash Flow Yield
Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income
Operating Profit
Expected 5 Year CAGR From Latest Actual
Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations
Capex
Tax Charge
Net Debt = Total Debt – Cash & Equivalents
EBIT

Numerator

Current Share Price
Current Share Price
Annualised Declared Cash Dividend
Cash Flow From Operations – Total Capex
EV = Current Share Price × Current Shares + Minority Equity + Net Debt +
Other LT Liabilities
Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Amortization
Shareholders' Equity
Sales
N/A
N/A

Denominator

Net Income
Depreciation
Pre-Tax Income
Total Equity
Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)
Shareholders' Equity / Current Basic Shares
Current Share Price
Market Cap = Current Share Price × Current Basic Shares
Sales

Basic EBIT + Depreciation + Amortization

IQmethodSM is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and valuations. The key features of **IQmethod** are: A consistently structured, detailed, and transparent methodology; Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

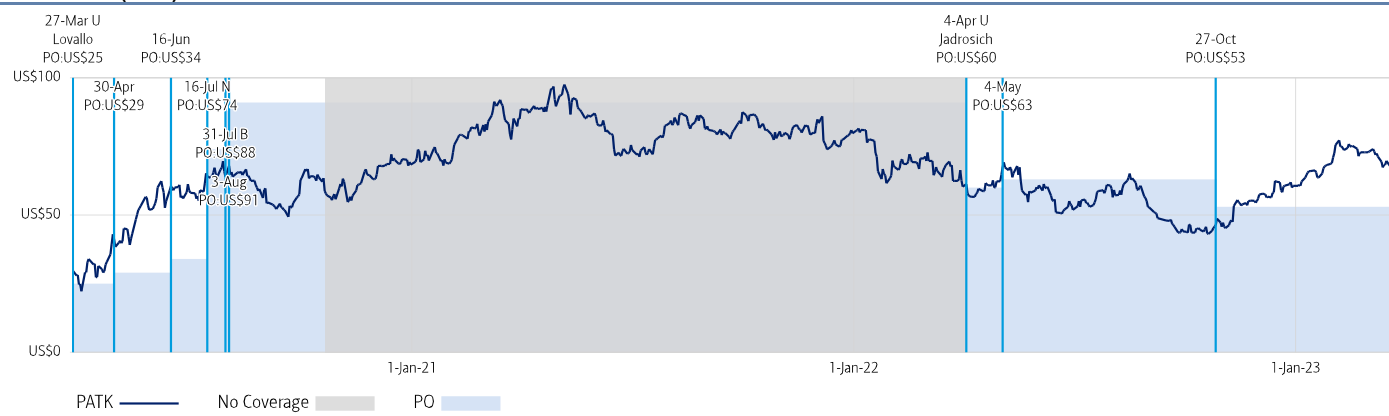
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Disclosures

Important Disclosures

Patrick Industries (PATK) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Building Group (as of 31 Dec 2022)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	39	46.43%	Buy	18	46.15%
Hold	17	20.24%	Hold	10	58.82%
Sell	28	33.33%	Sell	10	35.71%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2022)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1853	52.58%	Buy	1040	56.13%
Hold	840	23.84%	Hold	493	58.69%
Sell	831	23.58%	Sell	404	48.62%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

FUNDAMENTAL EQUITY OPINION KEY: Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. **VOLATILITY RISK RATINGS**, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. **INVESTMENT RATINGS** reflect the analyst's assessment of both a stock's absolute total return potential as well as its attractiveness for investment relative to other stocks within its *Coverage Cluster* (defined below). There are three investment ratings: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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