

Buy

Lennox International Inc. (LII)

Strong 3Q results, raising estimates and PT

| | | | |
|-----|-----------------------------------|------------------------|----------------------|
| LII | 12m Price Target: \$463.00 | Price: \$358.11 | Upside: 29.3% |
|-----|-----------------------------------|------------------------|----------------------|

Bottom line: Strong 3Q results, raising estimates and PT. LII reported 3Q23 segment EBIT that was +11% vs. Visible Alpha Consensus Data. The beat vs. VA consensus was primarily driven by higher than expected price/mix benefit in both Resi and Commercial segments (+\$51mn/+\$47mn price mix benefit to EBIT, respectively). Going forward, LII raised their FY23 adj. EPS guide to \$17.25-\$17.75 which we think could prove to be conservative (GS FY23 EPS of \$17.90) as price/mix benefits especially within the Commercial segment should aid another quarter of 20%+ margins in 4Q. Beyond FY23, we modestly raise our estimates as solid margin progression in Commercial and a bottom in the Resi HVAC cycle will be somewhat offset by uncertainty around timing of refrigerant related price increases and higher ramp-up costs for the new Commercial factory in Saltillo. Our FY23/FY24/FY25 EPS moves to \$17.90/\$19.60/\$21.75 (from \$17.30/\$19.35/\$21.50). We remain Buy rated on LII as Resi HVAC volumes are bottoming, the upcoming refrigerant change will aid pricing/margins over the next two years and there is further room for margin upside in Commercial. We raise our 12-month PT to \$463 (from \$455) which implies a 4.5-5.0% FY25 FCF yield.

What happened. LII reported 3Q23 adj. EPS of \$5.37. Segment EBIT was +11% vs. Visible Alpha consensus. Residential volume/price/mix was -2%/+2%/+7% while Commercial volume/price/mix was +2%/+10%/+3%. For FY23, LII raised the EPS guide to \$17.25-\$17.75 (from \$15.50-\$16.00) predicated on core revenue growth of ~5%.

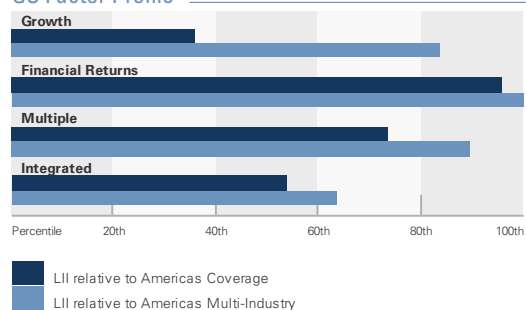
Estimate changes and valuation updates. We raise our FY23/FY24/FY25 EPS to \$17.90/\$19.60/\$21.75 (from \$17.30/\$19.35/\$21.50) on better margins and favorable mix. Our 12-month price target moves to \$463 (from \$455) as we roll forward

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Goldman Sachs & Co. LLC**Key Data**

Market cap: \$12.7bn
Enterprise value: \$14.2bn
3m ADTV: \$118.6mn
United States
Americas Multi-Industry
M&A Rank: 3

GS Forecast

| | 12/22 | 12/23E | 12/24E | 12/25E |
|----------------------------|----------------|----------------|----------------|----------------|
| Revenue (\$ mn) New | 4,718.4 | 4,994.5 | 5,208.1 | 5,485.7 |
| Revenue (\$ mn) Old | 4,718.4 | 4,935.4 | 5,146.3 | 5,420.6 |
| EBITDA (\$ mn) | 741.6 | 931.4 | 991.7 | 1,069.5 |
| EBIT (\$ mn) | 665.0 | 850.9 | 917.7 | 995.5 |
| EPS (\$) New | 14.08 | 17.90 | 19.60 | 21.75 |
| EPS (\$) Old | 14.08 | 17.30 | 19.35 | 21.50 |
| P/E (X) | 17.3 | 20.0 | 18.3 | 16.5 |
| Dividend yield (%) | 1.6 | 1.4 | 1.0 | 1.0 |
| Net debt/EBITDA (X) | 2.0 | 1.5 | 1.1 | 0.6 |
| | 9/23 | 12/23E | 3/24E | 6/24E |
| EPS (\$) | 5.37 | 3.56 | 3.09 | 6.37 |

GS Factor Profile

Source: Company data, Goldman Sachs Research estimates.
See disclosures for details.

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Buy

Lennox International Inc. (LII)

Rating since Oct 9, 2023

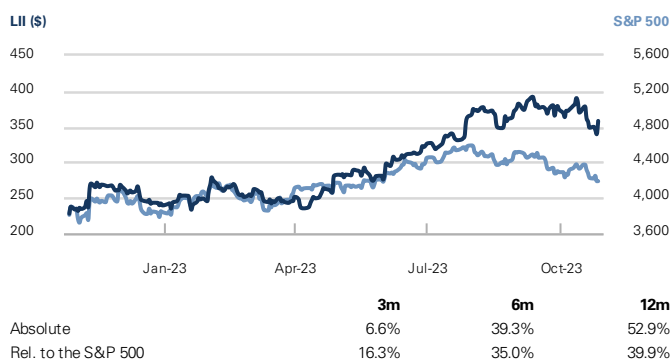
Ratios & Valuation

| | 12/22 | 12/23E | 12/24E | 12/25E |
|--------------------------|---------|--------|--------|--------|
| P/E (X) | 17.3 | 20.0 | 18.3 | 16.5 |
| EV/EBITDA (X) | 13.7 | 15.1 | 13.8 | 12.2 |
| EV/sales (X) | 2.2 | 2.8 | 2.6 | 2.4 |
| FCF yield (%) | 2.3 | 2.8 | 4.8 | 6.1 |
| EV/DACF (X) | 17.3 | 18.8 | 17.1 | 15.1 |
| CROCI (%) | 29.7 | 34.5 | 35.7 | 38.7 |
| ROE (%) | NM | NM | 185.8 | 96.8 |
| Net debt/EBITDA (X) | 2.0 | 1.5 | 1.1 | 0.6 |
| Net debt/equity (%) | (724.9) | 767.9 | 200.4 | 69.5 |
| Interest cover (X) | 17.2 | 15.6 | 17.6 | 19.1 |
| Inventory days | 67.2 | 80.0 | 78.8 | 79.0 |
| Receivable days | 43.2 | 47.2 | 48.4 | 46.0 |
| Days payable outstanding | 44.1 | 42.7 | 39.4 | 40.6 |

Growth & Margins (%)

| | 12/22 | 12/23E | 12/24E | 12/25E |
|----------------------|-------|--------|--------|--------|
| Total revenue growth | 12.5 | 5.9 | 4.3 | 5.3 |
| EBITDA growth | 10.1 | 30.8 | 14.1 | 7.8 |
| EPS growth | 11.8 | 27.1 | 9.5 | 10.9 |
| DPS growth | 17.0 | 29.7 | (33.4) | 3.0 |
| Gross margin | 27.2 | 31.4 | 32.0 | 32.5 |
| EBIT margin | 14.1 | 17.0 | 17.6 | 18.1 |

Price Performance



Source: FactSet. Price as of 26 Oct 2023 close.

Income Statement (\$ mn)

| | 12/22 | 12/23E | 12/24E | 12/25E |
|---------------------------------------|--------------|--------------|--------------|----------------|
| Total revenue | 4,718.4 | 4,994.5 | 5,208.1 | 5,485.7 |
| Cost of goods sold | (3,433.7) | (3,427.2) | (3,543.4) | (3,703.4) |
| SG&A | (621.5) | (716.4) | (747.1) | (786.8) |
| R&D | 0.0 | 0.0 | 0.0 | 0.0 |
| Other operating inc./exp.) | 1.7 | - | - | - |
| EBITDA | 665.0 | 869.4 | 991.7 | 1,069.5 |
| Depreciation & amortization | 0.0 | (18.5) | (74.0) | (74.0) |
| EBIT | 665.0 | 850.9 | 917.7 | 995.5 |
| Net interest inc./exp.) | (38.7) | (54.4) | (52.0) | (52.0) |
| Income/(loss) from associates | - | - | - | - |
| Pre-tax profit | 625.3 | 794.0 | 861.7 | 939.5 |
| Provision for taxes | (121.7) | (156.7) | (172.9) | (186.9) |
| Minority interest | - | - | - | - |
| Preferred dividends | - | - | - | - |
| Net inc. (pre-exceptionals) | 503.6 | 637.4 | 688.8 | 752.6 |
| Net inc. (post-exceptionals) | 503.6 | 637.4 | 688.8 | 752.6 |
| EPS (basic, pre-except) (\$) | 14.12 | 17.98 | 19.71 | 21.87 |
| EPS (diluted, pre-except) (\$) | 14.08 | 17.90 | 19.60 | 21.75 |
| EPS (ex-ESO exp., dil.) (\$) | -- | -- | -- | -- |
| DPS (\$) | 3.98 | 5.16 | 3.44 | 3.54 |
| Div. payout ratio (%) | 28.2 | 28.7 | 17.5 | 16.2 |
| Wtd avg shares out. (basic) (mn) | 35.7 | 35.4 | 34.9 | 34.4 |
| Wtd avg shares out. (diluted) (mn) | 35.8 | 35.6 | 35.1 | 34.6 |

Balance Sheet (\$ mn)

| | 12/22 | 12/23E | 12/24E | 12/25E |
|---------------------------------------|----------------|----------------|----------------|----------------|
| Cash & cash equivalents | 52.6 | 37.4 | 324.2 | 751.1 |
| Accounts receivable | 608.5 | 684.2 | 697.9 | 685.7 |
| Inventory | 753.0 | 749.2 | 781.2 | 822.9 |
| Other current assets | 73.9 | 158.1 | 158.1 | 158.1 |
| Total current assets | 1,488.0 | 1,628.9 | 1,961.4 | 2,417.8 |
| Net PP&E | 548.9 | 708.6 | 784.6 | 830.6 |
| Net intangibles | 186.3 | 181.7 | 181.7 | 181.7 |
| Total investments | 0.0 | 0.0 | 0.0 | 0.0 |
| Other long-term assets | 335.9 | 363.9 | 363.9 | 363.9 |
| Total assets | 2,567.6 | 2,883.1 | 3,291.6 | 3,794.0 |
| Accounts payable | 427.3 | 374.6 | 390.6 | 433.4 |
| Short-term debt | 710.6 | 361.6 | 361.6 | 361.6 |
| Current lease liabilities | 63.3 | 60.2 | 60.2 | 60.2 |
| Other current liabilities | 394.5 | 477.7 | 494.7 | 516.9 |
| Total current liabilities | 1,595.7 | 1,274.0 | 1,307.1 | 1,372.1 |
| Long-term debt | 814.2 | 1,081.6 | 1,081.6 | 1,081.6 |
| Non-current lease liabilities | 161.8 | 162.5 | 162.5 | 162.5 |
| Other long-term liabilities | 199.0 | 181.9 | 181.9 | 181.9 |
| Total long-term liabilities | 1,175.0 | 1,426.0 | 1,426.0 | 1,426.0 |
| Total liabilities | 2,770.7 | 2,700.0 | 2,733.1 | 2,798.1 |
| Preferred shares | - | - | - | - |
| Total common equity | (203.1) | 183.1 | 558.5 | 995.9 |
| Minority interest | - | - | - | - |
| Total liabilities & equity | 2,567.6 | 2,883.1 | 3,291.6 | 3,794.0 |
| BVPS (\$) | (5.68) | 5.14 | 15.89 | 28.78 |

Cash Flow (\$ mn)

| | 12/22 | 12/23E | 12/24E | 12/25E |
|---------------------------------------|----------------|----------------|----------------|----------------|
| Net income | 503.6 | 637.4 | 688.8 | 752.6 |
| D&A add-back | 77.9 | 80.5 | 74.0 | 74.0 |
| Minority interest add-back | - | - | - | - |
| Net (inc)/dec working capital | (267.9) | (111.7) | (12.6) | 35.5 |
| Others | (4.8) | 64.0 | 6.8 | 6.8 |
| Cash flow from operations | 302.3 | 604.9 | 757.0 | 868.9 |
| Capital expenditures | (101.1) | (250.0) | (150.0) | (120.0) |
| Acquisitions | - | - | - | - |
| Divestitures | 1.6 | 1.6 | - | - |
| Others | (3.5) | (1.1) | - | - |
| Cash flow from investing | (103.0) | (249.5) | (150.0) | (120.0) |
| Dividends paid | (142.0) | (183.0) | (120.2) | (121.9) |
| Share issuance/(repurchase) | (296.4) | (72.1) | (200.0) | (200.0) |
| Inc/(dec) in debt | 272.6 | (92.6) | - | - |
| Others | (11.7) | (23.0) | - | - |
| Cash flow from financing | (173.8) | (360.1) | (320.2) | (321.9) |
| Total cash flow | 21.8 | (15.3) | 286.8 | 426.9 |
| Free cash flow | 201.2 | 354.9 | 607.0 | 748.9 |
| Free cash flow per share (basic) (\$) | 5.64 | 10.01 | 17.37 | 21.76 |

Source: Company data, Goldman Sachs Research estimates.

our Q5-Q8 EBITDA estimates. Our price target is based on 17.0 (vs. 17.5x prior) our Q5-Q8 EBITDA given the recent de-rating across our coverage.

Key Risks. Slowdown in Resi replacement demand; softness in Commercial given tighter credit backdrop; pricing realization on refrigerant change does not fully materialize.

Disclosure Appendix

Reg AC

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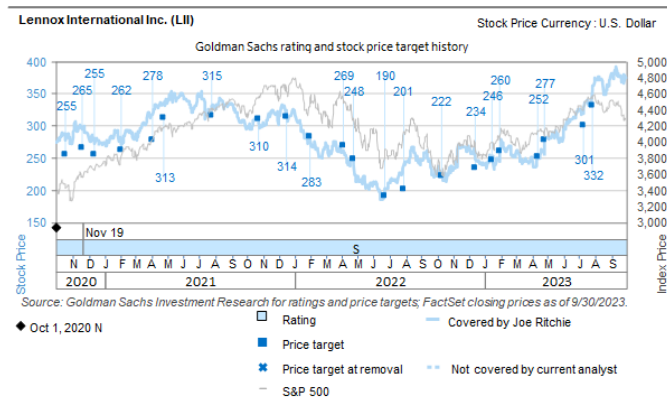
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|--------|---------------------|------|------|--|----------------------------------|------|------|
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