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## Financial Analysis and Valuation of Hawkins Inc.

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# Hawkins, Inc.

## HWKN / NASDAQ

### *Initiating Coverage*

### Investment Rating: Sell

PRICE: USD 43.56 S&P 500: 3,066.91 DJIA: 27,347.36 RUSSELL 2000: 1,589.33

- Hawkins, Inc. declared a quarterly cash dividend of USD 0.23 per share (USD 2.45 million) on October 31, 2019
- Hawkins entered the Health and Nutrition market with the acquisition of Stauber Specialty Ingredients in 2015 – its largest acquisition in the company’s history
- The newest addition to Hawkins’ product line is a series of beer souring agents curated by Hawkins themselves

Valuation	2019 A	2020 E	2021 E
EPS (USD)	\$2.75	\$3.66	\$3.86
P/E	<u>17.24</u>	10.86	10.93
P/CFPS	8.23	8.53	8.52
P/BVPS	27.77	28.01	28.62
EV/EBITDA	8.53	10.77	9.73

\*The actual figures in this chart are from Yahoo!Finance as of November 1, 2019

#### Market and Trading Information

Equity Market Cap (USD) (M):	468.598	52-Week Range (USD):	32.79 - 47.94
Enterprise Value (USD)(M):	543.09	12-Month Stock Return:	36.17%
Shares Outstanding (M):	10.58	Dividend / Capital Gain Yields	2.31/33.86%
Estimated Float (M):	9.57	12-Month Russell 2000 Return:	6.73%
3-mo Avg. Daily Volume (M):	87,401	Beta:	1.07

#### Company Quick View:

**Location:** 2381 Rosegate, Roseville MN, 55113

**Industry:** Chemicals and allied products, SIC 5169 / Other Chemical and Allied Products Merchant Wholesaler, NAICS 424690

**Description:** Hawkins, Inc. distributes, blends and manufactures bulk and specialty chemicals and other health and nutrition products for its customers in a wide variety of industries. Headquartered in Roseville, Minnesota, and with 41 facilities in 19 states, the Company creates value for its customers through superb customer service and support, quality products and personalized applications

**Key Products & Services:** Industrial, Water Treatment, Health and Nutrition

**Website:** <http://www.hawkinsinc.com>

**Analyst:** Samantha Alvarado



## STOCK PRICE PERFORMANCE

Figure 1: 5-year Stock Price Performance



Hawkins, Inc. (HWKN) closed on the NASDAQ at USD 43.56 per share on November 1, 2019. The stock took a sharp turn downwards during October 2019, but has made a recovery as the company released its rosy second quarter reports. The 52-week range of the stock is USD 32.79 – 47.94. Year-to-date, Hawkins has had a return of 5.73 percent, while its closest industry competitor, Innophos Holdings, has earned a return of 37.30 percent. From November 1, 2018 to this report date, the company stock has seen a return of 18.54 percent. Hawkins earned a higher return than Innophos Holdings and the Russell 2000 with 12-month return of 11.44 percent and 4.28 percent, respectively. Hawkins' five-year annual return is 2.89 percent, which is above Innophos Holdings' return of -1.88 percent. The Russell 2000 has a return of 8.93 percent over the same time. Hawkins, Inc. has a history of outperforming the return of its competitors, however, has fallen short of Innophos' growth since January.

## INVESTMENT DECISION SUMMARY

Using a corporate valuation model that discounts free cash flows at the average cost of funding (WACC), I have forecasted an intrinsic value as of 11/1/2019 of USD 33.79. Given the current economic conditions, the sales growth of the company has softened. However, their most recent quarterly report has shown that their gross profit margins have improved slightly over previous years due to favorable pricing in the commodities markets. Their mix of debt and equity financing is the driving factor behind the lower intrinsic value than market. Only 15 percent of the firm is financed with debt, and 85 percent of the firm is financed through equity. Equity is the more costly financing at 9.42 percent. After conducting this analysis, I recommend that investors sell Hawkins, Inc. stock because the intrinsic value of the stock I have forecasted is more than 10 percent below the market price. While this price is within the 52-week range, the standard deviation of the monthly returns of the stock is 9 percent, and the intrinsic value I calculated is more than one standard deviation from the mean return.

## COMPANY DESCRIPTION

Hawkins, Inc., a manufacturer, distributor, and blender of chemicals and ingredients, was incorporated in the state of Minnesota in 1938. It was reincorporated in Minnesota in 1955 as Hawkins Chemical, Inc., and has been operating under the current name since 2001. The firm went public in 1985. Executive operations are based out of Roseville, Minnesota. As of March 31, 2019, Hawkins had 657 employees.

Hawkins has a long history of acquisitions of existing companies and their assets. In the 1970s and 1980s Hawkins acquired six companies: Vel-Tex Chemical (1971), The Lynde Co. (1972), Feed-Rite Controls, Inc. (1976), Mon-Dak Chemical Inc. (1979), Dakota Chemical, Inc. (1982), and Tessman Seed, Inc. (1989). In 1993, Hawkins acquired Industrial Chemical & Equipment Co., which operated as the industrial segment of the Hawkins business. In 1998, Hawkins merged three of its subsidiaries to form the water treatment segment of their business. Since 2000, Hawkins has acquired certain assets from St. Mary's Chemical (2000), all of the assets of Trumark, Inc. (2007), Advanced Chemical Solutions, Inc. (2013), The Dumont Company, Inc. (2014), and Davis Supply, Inc. (2015), as well as completing the total acquisition of Vertex Chemical Corporation (2011), Novel Wash Co. Inc. (2011), R.H.A. Corporation (2011), and Stauber Performance Ingredients (2015).

Hawkins operates in three market segments: industrial, water treatment, and health and nutrition. The largest of the three segments, the industrial segment, focuses on industrial chemicals, products, and services to the agricultural, chemical processing, electronics, energy, food, pharmaceutical, and plating industries. The segment's principal products are acids, alkalis, and industrial and food-grade salts. Activities of the industrial group include receiving, storing and distributing various bulk chemicals, repackaging water treatment chemicals for its water treatment segment and bulk industrial chemicals for resale in smaller quantities, custom blending of chemicals for customers, and bleach packaging. The segment's products are sold in the food and pharmaceutical markets nationally. The group's sales are primarily focused in Illinois, Iowa, Kentucky, Minnesota, Missouri, North Carolina, North Dakota, South Dakota, Tennessee, and Wisconsin.

The Hawkins water treatment segment provides chemicals, equipment and solutions for potable water, municipal and industrial wastewater, industrial process water, and non-residential swimming pool water. The segment primarily services customers in Florida, Illinois, Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, South Dakota and Wisconsin.

The health and nutrition segment is the smallest of the three segments. This segment provides ingredient distribution, processing, and formulation solutions to manufacturers of nutraceutical, functional food and beverage, personal care, dietary supplement and other nutritional food, health, and wellness products. The segment provides products such as minerals, botanicals and herbs, vitamins and amino acids, excipients, joint products, sweeteners and enzymes. The segment's wide range of products combined with services and solutions for its customer positions this segment as a one-stop ingredient solutions provider. This segment's products are

sold nationally, as well as internationally. The segment operates facilities in California and New York.

## **MANAGEMENT AND CORPORATE GOVERNANCE**

The executive leadership team of Hawkins, Inc. consists of the following members:

### **Patrick Hawkins, Chief Executive Officer and President**

Hawkins joined the company in 1992 and has served as Business Director of Food Pharmaceuticals, Business Manager of Food and Co-Extrusion Products, Sales Representative for Food Ingredients, Plant Manager, Quality Director, Technical Director, and various other positions. He has been President since 2010 and CEO since 2011.

### **Jeffrey Oldenkamp, Vice President, Chief Financial Officer, Treasurer**

Oldenkamp joined the company in 2017 as Chief Financial Officer, and assumed the role of Vice President and Treasurer later that year. Prior to working with Hawkins, he served as Vice President of Finance, and later Chief Financial Officer, at MTS Systems Corporation, a supplier of high-performance test systems and sensors, and served as Americas Operations Chief Financial Officer and Vice President with Nilfisk-Advance, Inc, a global manufacturer of professional cleaning equipment.

### **Richard Erstad, Vice President, General Counsel, Secretary**

Erstad joined the company in 2008 as Vice President, General Counsel, and Secretary. Erstad is a member of the Minnesota BAR. Prior to working with Hawkins, he served as General Counsel and Secretary of BUCA, Inc., a restaurant company and as an attorney with the corporate group of Faegre & Benson LLP, a law firm, where he focused on securities law, and mergers and acquisitions.

### **Thomas Keller, Vice President – Water Treatment Group**

Keller joined the company in 1980, holding various positions, most recently as Water Treatment General Manager. He has held his title as Vice President – Water Treatment Group since 2012.

### **Shirley Rozeboom, Vice President – Health and Nutrition**

Rozeboom joined the company as a part of the Stauber acquisition in 2015. At Stauber, she held positions as Senior Vice President of Sales, Director of Sales, and Account Executive. She was named Vice President – Health and Nutrition in April 2019, replacing Daniel Stauber, who held this role through March 31, 2019.

Incentive compensation across all executives is reliant in part to pre-tax income. For executives in charge of a business unit, an operational measure of business profitability is a determinant in their incentive compensation. Each executive also has individual determinants of their incentive compensation. No incentive is paid unless 80 percent of each determinant is achieved. The

Compensation Committee of the Board of Directors has discretion to adjust the final payouts of the program.

For the Chief Executive Officer, Chief Financial Officer, and General Counsel, incentive compensation is based 80 percent on the corporate performance against the pre-tax income goal and 20 percent on meeting their individual goals. The Chief Executive Officer's individual determinants include overseeing strategic direction matters, business expansion matters, and operational efficiency initiatives. Chief Financial Officer individual determinants include business efficiency and support, overseeing significant information technology initiatives, and talent management and engagement initiatives.

For those executives in charge of a business unit, their incentive compensation is based 40 percent on company-wide performance, 40 percent on business segment operational measure of business profitability, and 20 percent on individual objectives. For the Vice President – Health and Nutrition, the business unit measure is based on the EBITDA performance of that segment and the individual determinants include business expansion initiatives. The Vice President – Water Treatment Group has a business unit compensation that measure product sales less the cost of material including freight in and the selling costs as compared to a targeted level of operational profitability for the period. Individual determinants for the Water Treatment Group include business expansion initiatives.

There are additional annual equity incentive compensation programs available for executives that grant performance-based restricted stock units that would vest based on company performance during the current fiscal year and would be settled in share of restricted stock that would vest after two more years of service.

The following table shows the members of the Board of Directors, their positions and experience:

<b>Board of Directors</b>	<b>Positions</b>	<b>Experience</b>
John S. McKeon	Chairman of Board, Governance and Nominating Committee	Retired President & CEO of ConAgra Foods, Inc. Venture Development Group
Patrick Hawkins		Current Chief Executive Officer of Hawkins, Inc.
Mary Schumacher	Audit Committee, Compensation Committee	Retired Chief Operating Officer of Twin Cities Habitat for Humanity
Daniel Stauber		Retired Vice President of Health and Nutrition and President of Stauber Performance Ingredients, Inc.

James Faulconbridge (Independent)	Audit Committee, Compensation Committee, Governance and Nominating Committee (Chair)	Current President of Karges- Faulconbridge, Inc.
Duane Jergenson (Independent)	Compensation Committee	Retired Vice President of Operations of Taylor Corporation
Daryl Skaar (Independent)	Audit Committee, Compensation Committee	Retired Vice President and Chief Procurement Officer of Lucent Technologies
James Thompson (Independent)	Compensation Committee (Chair), Governance and Nominating Committee	Board member of Sims Metal Management
Jeffrey Wright (Independent)	Audit Committee (Chair), Compensation Committee, Governance and Nominating Committee	Retired Chief Financial Officer of G&K Services

Hawkins has low diversity in terms of gender; only one director is female. Age diversity is moderate; all members (if their ages are provided) are between ages 48 and 77.

Hawkins, Inc.'s ISS Governance QualityScore as of October 4, 2019 is 3. The pillar scores are Audit: 1; Board: 5; Shareholder Rights: 2; Compensation: 4. Corporate governance scores are from Institutional Shareholder Services (ISS). Scores indicate decile rank relative to index or region. A score of 1 indicates low governance risk; a 10 indicates high governance risk.

## ACCOUNTING QUALITY AND POLICIES

Hawkins, Inc. partners with the Minneapolis branch of KPMG for their auditing services. KPMG has been auditing Hawkins' annual SEC filings since 2010. KPMG issued an unqualified opinion on Hawkins' 2019 financial statements. In reviewing Note 1 to the financial statements regarding significant accounting policies, I found the following comments made by the auditors significant:

- Hawkins inventory consists primarily of finished goods, valued at the lower of cost or net realizable value. 69 percent of the cost of inventory is determined using the last-in, first-out (LIFO) method, and the other 31 percent is valued using first-in, first-out (FIFO).
- There were no goodwill impairments found during the 2019 fiscal year. In 2018, there was a goodwill impairment charge for USD 39.1 million related to the Health and Nutrition reporting unit. The impairment was a result of changes in expectations for

future growth as part of long-term strategic planning to align historical experience with expected changes in future product mix.

To determine if the accounting policies of Hawkins may be distorting the earnings of the company, I have calculated the quality of earnings ratio. In 2019, the ratio is 1.83, and over the last five years, the ratio has averaged 1.78. This quality of earnings ratio tells us that the net income for the firm is supported by appropriate operating cash flows.

## SHAREHOLDER ANALYSIS

According to the Hawkins' SEC quarterly filing, as of September 30, 2019, Hawkins has 10,757,538 million shares outstanding. Institutional ownership is at 59.51 percent, with a total of 6,349,717 shares held. The top five institutional holders of the stock, reported as of June 19, 2019, are as follows:

Owner Name	Shares Held	Percent held
Blackrock Inc.	1,443,370	13.53%
Vanguard Group Inc.	750,042	7.03%
Price T. Rowe Associates Inc.	613,239	5.75%
Dimensional Fund Advisors LP	612,234	5.74%
State Street Corp	272,997	2.56%

During the last twelve months, there have been 24 insider trades – 16 open market buys and 8 sells. On July 31, 2019, all directors acquired 1,144 shares, and on May 23, 2019, all officers acquired shares per their compensation packages. All eight dispositions were made by Hawkins officers and are as follows:

Insider	Date	Shares Sold
Daniel Stauber	4/2/2019	365
Thomas Keller	4/2/2019	1,163
John Sevenich	4/2/2019	1,168
Theresa Moran	4/2/2019	656
Richard Erstad	4/2/2019	1,311
Patrick Hawkins	4/2/2019	2,909
Daniel Stauber	4/1/2019	995
Thomas Keller	11/16/2018	100



On February 7, 2019, Hawkins announced that the Board of Directors increased the number of shares authorized to be repurchased under its share repurchase program by 500,000 shares of outstanding common stock. The primary objective of the program is to offset the impact of dilution from issuances relating to employee and director equity grants and the company's employee stock repurchase program. Since the time of the announcement, the board has not stated a deadline for this stock repurchase.

## **INDUSTRY ANALYSIS**

Hawkins, Inc. is a part of chemicals and allied products industry with the SIC 5169 and NAICS 424690. As listed on osha.gov, establishments in this industry are primarily engaged in the wholesale distributions of chemicals and allied products such as acids, industrial and heavy chemicals, dyestuffs, industrial salts rosin, and turpentine.

The chemicals and allied products industry is large, with roughly 12,500 establishments that earn a combined USD 200 billion in annual revenue, per Dun & Bradstreet's research. Hawkins market share in this industry is roughly 0.27 percent. According to the US Statistics of US Businesses (SUSB) 2016 census, there are 3,071 establishments with 500 or more employees – a similar operations size to Hawkins - in this NAICS code. Each firm's ability to compete within the industry is tied closely to product price, product performance, product quality, product availability and security of supply, breadth of product offerings, geographic reach, and ability to create product innovations, technical expertise and customer service.

Product pricing and product availability can be challenges for the industry. The commodities markets can be volatile and cyclical in nature, which can affect negatively a firm's ability to price competitively and decrease their product profit margins. Contracts with suppliers are important in keeping product costs down, although that is not always a guarantee.

Size and geographic reach contribute to the competitive nature of the industry. Larger companies may be able to provide large product lines, secure better supply contracts, reach larger geographic areas, create larger distribution networks, and enjoy other economies of scale. Smaller, local or regional companies, like Hawkins, compete effectively by providing superior service and solutions or geographical focus. Hawkins' mission statement highlights this focus on customer services and solutions: "Our mission is to supply high quality products and innovative solutions with an exceptional level of customer service."

## **INVESTMENT RISK**

Hawkins Inc. deals with volatility in the price and availability of their products. There are regular and reoccurring fluctuations in the pricing of raw materials such as caustic soda. The cyclical nature of raw materials commodities is a result of fluctuations in the supply of the material. There is always the added concern of long lead times, limits, or cutoffs in supply. To help smooth out the cost of these raw materials, Hawkins has contracts with suppliers where prices

paid adjust quarterly or monthly. However, the prices paid under these contracts can lag behind the market prices of the raw materials. This can lead to inventory values that exceed the current market pricing and puts product margins at risk.

The chemicals and allied products industry need to comply with many local, state, and federal regulations. Violation of any of these laws could lead to significant unexpected costs, loss of capacity to generate revenues, and increase the cost of doing business. In their health and nutrition segment, Hawkins must abide by the Food and Drug Administration's (FDA) regulations. The risk of recalls and discontinuations of products, as well as the additional costs of required record-keeping, expanded documentation and labelling and additional scientific substantiation, are a relevant concern for this segment. While there is the risk, there have been no disclosed recalls of any Hawkins products.

The chemicals Hawkins handles can also be hazardous, toxic, or volatile under local, state, and federal law that pose a substantial environmental and safety risk. Hazards common to chemical and allied products include explosions, fires, mechanical failures, traffic accidents, and environmental contamination. Hawkins disclosed in their 2019 10-K that groundwater contamination does exist at one of their facilities, and they accrued USD 0.6 million for remediation of this contamination. This is Hawkins' only disclosed environmental or safety event.

## PEER ANALYSIS

The following chart includes companies in the chemicals and allied products industry (SIC 5169):

Company	Ticker Symbol	Sales in USD (million)	Market Cap in USD (million)	PE Ratio	EV / EBITDA	Debt / Assets	ROA (%)	ROE (%)
Hawkins, Inc	HWKN	\$549M	\$483M	17.67	9.07	0.44	6.33	12.06
Innophos Holdings	IPHS	\$759M	\$623M	29.79	9.06	0.59	4.89	6.30
United Guardian, Inc.	UG	\$12.9M	\$83M	20.34	16.13	0.13	23.49	37.76
Univar Solutions	UNVR	\$9.1B	\$4.35B	14.70**	11.18	0.77	4.36	-3.31
Ashland Global Holdings, Inc	ASH	\$3.7B	\$4.75B	47.53	11.41	0.58	2.67	2.45

\*The figures in this chart are as of November 9, 2019. Debt / Asset ratio is calculated using most recent audited financial statements.

\*\*Trailing P/E was not available. Forward P/E was used here.

I chose the peers in this analysis because they share similar product lines with Hawkins, Inc., and they all operate in the same industry.

Through its subsidiaries, Innophos Holdings produces specialty ingredient solutions for the food, health, nutrition, and industrial markets. The company operates in three segments: Food, Health and Nutrition; Industrial Specialties; and Co-Products and Other. The company's products have applications in the food, beverage and dietary supplement end markets.

United Guardian manufactures and markets cosmetic ingredients, personal care products, pharmaceuticals, medical lubricants, health care products, and industrial products. The company also takes part in R&D for cosmetic and personal care products. United Guardian operates in one business segment with four separate product categories: personal care products, pharmaceuticals, medical products, and industrial products.

Univar Solutions is a chemical and ingredients distributor and provider of specialty services. The company purchases chemicals and warehouses, repackages, blends, dilutes, transports and sells those products to their customers. They also provide value-added, specialty solutions including e-commerce and digital marketing and storage solutions for its customers. The company operates in four geographical segments: Univar USA, Univar Canada, Univar Europe and the Middle East and Africa, and Rest of World.

Ashland Global Holdings provides specialty chemical solutions to customers in a range of consumer and industrial markets that include adhesives, architectural coatings, construction, energy, food and beverage, personal care and pharmaceutical. The company operates within three segments: Specialty Ingredients, Composites and Intermediates, and Solvents.

## **HISTORICAL FINANCIAL ANALYSIS**

I decided to compare Hawkins, Inc. with Innophos Holdings. They have a similar market capitalization and operate in similar segments. Innophos' segments include Food, Health and Nutrition, Industrial Specialties, and Other; the "Other" segment includes fertilizers and manufacturing products. While there is a slight difference in the segments, there are no two companies in this industry that operate in identical segments. Innophos has a fiscal year end of December 31 and Hawkins has a fiscal year end of March 31. While Hawkins states that there is some cyclicity in the price and availability of their products, that factor would be too complex to take into account for purposes of this report. For the purpose of this report, I consider the difference in timing of the reports immaterial.

### **Productivity Ratios**

Hawkins has grown in sales over the last four reporting periods ranging from 4.3% to 16.8% per year. Innophos generated positive sales growth during its most recent year and decreases in sales in the three of the last four years. Hawkins has consistently had a higher inventory turnover ratio than Innophos, averaging about 8.58 times in the last five years over Innophos' average of 3.9. I partially attribute the difference to dissimilar operating segments. Hawkins' higher turnover has

translated into a higher operating working capital turnover as well. Hawkins has maintained an average operating working capital turnover of over 5.26 for the last five years, while Innophos has averaged 3.86 over the same period.

Hawkins' assets are performing better than Innophos over this period. Its operating working capital performance, long-term, and net fixed asset turnover perform above Innophos'. In three of the last five years, Hawkins has a higher invested capital turnover than Innophos.

	<b>Productivity Ratios</b>				
	<b>2019</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
HWKN Growth in sales	10.3%	4.3%	16.8%	13.7%	N/A
IPHS Growth in sales	11.1%	-0.5%	-8.1%	-6.0%	N/A
HWKN Inventory turnover	8.49	7.72	9.17	7.98	8.55
IPHS Inventory turnover	4.45	4.96	5.65	4.57	4.55
HWKN Operating working capital turnover	5.49	5.43	6.28	4.26	4.84
IPHS Operating working capital turnover	4.41	3.87	3.86	4.07	3.10
HWKN Net fixed asset turnover	2.01	1.79	1.52	1.35	3.02
IPHS Net fixed asset turnover	1.64	1.49	2.02	2.10	2.35
HWKN Invested capital turnover	1.47	1.35	1.22	1.02	1.86
IPHS Invested capital turnover	1.20	1.07	1.32	1.39	1.34

\*Innophos' fiscal year end is December 31. The data labelled 2019 is for their fiscal year ended December 13, 2018.

### Liquidity Ratios

Hawkins, Inc. and Innophos Holdings have similar current and quick ratios. In the most recent reporting year, Hawkins had a current ratio of 2.54 while Innophos had 2.25 as their current ratio. This is due to Innophos' higher inventory as a percent of current assets; they increased their inventory in 2019 to support their transition to a value-chain business model. In prior years, each company's level of inventory held to support their business is the factor that determines who holds the higher current ratio. Hawkins's quick ratio was 1.49 and Innophos's is 1.01 in the most recent reporting year. In 2017 and 2018, Hawkins had a lower quick ratio because of lower cash reserves which was a result of increases in their debt repayments and capital expenditures after the acquisition of Stauber. The reason Innophos's quick ratio fell in 2019 is that Innophos had a USD 10 million increase in their accounts payable due to an increase in customer demand.

Hawkins average operating cycle for the last five years is 88 days and its cash cycle averages 66 days over the same period. This two are significantly lower than Innophos'. Hawkins is able convert their products to cash from customers, on average, 25 days faster than Innophos is. This could be a result of differing credit terms with vendors and customers.

	<b>Liquidity Ratios</b>				
	<b>2019</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
HWKN Current ratio	2.73	2.44	2.29	2.85	3.96
IPHS Current ratio	2.25	2.64	2.98	2.82	3.90
HWKN Quick ratio	1.49	1.31	1.31	1.80	2.56
IPHS Quick ratio	1.01	1.36	1.63	1.16	1.90

HWKN Cash ratio	0.17	0.09	0.13	0.40	1.10
IPHS Cash ratio	0.14	0.25	0.56	0.17	0.39
HWKN Operating cycle	84.96	93.27	83.05	97.98	83.14
IPHS Operating cycle	128.72	124.61	103.65	116.75	119.68
HWKN Cash cycle	65.73	69.07	60.59	71.42	63.01
IPHS Cash cycle	92.30	89.00	77.68	99.68	96.57

\*Innophos' fiscal year end is December 31. The data labelled 2019 is for their fiscal year ended December 31, 2018.

### Financial Risk (Leverage) Ratios

Hawkins uses less debt to finance their operations. Hawkins' debt to equity ratio has been decreasing for the last four years, from 1.09 to 0.65. The increase in fiscal year 2016 was due to the capital needed for their acquisition of Stauber Performance Ingredients. Since then, they have made it a point to decrease the financial debt they hold by increasing their debt repayments. Innophos' debt to equity ratio has been increasing over the last three years from 0.55 to 1.43. During 2018, Innophos entered into a new credit agreement that increased their revolving credit from USD 400 million to USD 650 million, which they have been using to make their transition to the value-chain business model. Due to the lower level of debt that Hawkins has, their interest expense is much lower than Innophos'. This has allowed them to maintain a much higher interest coverage ratio – both accounting based and cash based.

	Financial Risk (Leverage) Ratios				
	2019	2018	2017	2016	2015
HWKN Debt-to-equity ratio	0.65	0.80	0.83	1.09	0.27
IPHS Debt-to-equity ratio	1.43	1.35	0.85	1.01	0.55
HWKN Financial debt-to-equity ratio	0.35	0.45	0.45	0.63	0.03
IPHS Financial debt-to-equity ratio	0.92	0.96	0.55	0.67	0.32
HWKN Interest coverage ratio (accounting)	10.99	9.85	15.40	26.78	72.94
IPHS Interest coverage ratio (accounting)	5.28	10.20	11.26	7.78	26.14
HWKN Interest coverage ratio (cash)	15.24	14.21	18.06	33.46	89.30
IPHS Interest coverage ratio (cash)	7.55	14.76	15.20	11.98	33.38
HWKN Financial debt over total assets	0.21	0.25	0.25	0.30	0.03
IPHS Financial debt over total assets	0.38	0.41	0.30	0.33	0.20

\*Innophos' fiscal year end is December 31. The data labelled 2019 is for their fiscal year ended December 31, 2018.

### Profitability and Valuation Ratios

In the last five fiscal years, Hawkins has had significantly lower gross profit, EBITDA, and NOPAT margins than Innophos', with the exception of 2016 NOPAT margin. Hawkins' 2016 NOPAT margin was an anomaly because the acquisition of Stauber Performance Ingredients included intangible assets that were deductible for income tax purposes, which allowed for Hawkins to record a USD 28.6 million deferred tax liability in that year. Hawkins' 2016 ROIC value of 27.33 percent is a result of the deferred tax liability. Without the effect of this entry, all else held equal, the ROIC for Hawkins would be roughly 13 percent.

Both the return on equity ratio and return on assets ratios see a dramatic drop in 2018. In fiscal 2018, Hawkins saw a tax benefit as a result of the US Tax Cuts and Jobs Act of 2017, which lowered the tax rate to 21 percent for corporations. In addition to the tax change, Hawkins also had a goodwill impairment charge for USD 39.1 million related to the Health and Nutrition reporting unit. The impairment was a result of changes in expectations for future growth as part of long-term strategic planning to align historical experience with expected changes in future product mix. Without the effect of the goodwill impairment, all else held equal, the return on assets for 2018 would be 8.6 percent, and return on equity would be 14.4 percent.

	<b>Profitability/Valuation Ratios</b>				
	<b>2019</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
HWKN Gross profit margin	21.1%	22.5%	24.0%	22.8%	23.2%
IPHS Gross profit margin	23.5%	26.2%	25.9%	23.0%	26.9%
HWKN EBITDA margin	10.5%	10.8%	11.9%	11.1%	13.6%
IPHS EBITDA margin	12.7%	14.3%	16.1%	11.4%	17.3%
HWKN NOPAT margin	5.6%	5.4%	7.1%	12.9%	11.5%
IPHS NOPAT margin	8.1%	4.8%	8.3%	3.9%	10.7%
HWKN Return on assets	6.9%	0.2%	7.3%	5.1%	15.7%
IPHS Return on assets	8.3%	8.8%	13.0%	8.6%	15.8%
HWKN Return on equity	11.4%	0.3%	13.3%	10.7%	14.1%
IPHS Return on equity	13.3%	8.5%	15.0%	9.6%	15.2%
HWKN Return on invested capital	8.40%	6.93%	8.43%	27.33%	N/A
IPHS Return on invested capital	9.23%	6.05%	10.34%	4.91%	N/A

\*Innophos' fiscal year end is December 31. The data labelled 2019 is for their fiscal year ended December 13, 2018.

## PROSPECTIVE FINANCIAL ANALYSIS

Based on the quarterly data from the 2019, Hawkins has seen a slowing in sales over the last five quarters and their second quarter results saw a drop in sales of 3.63 percent over the same period in the prior year. This appears to be a common theme in its competitors – Innophos Holdings, United Guardian, and Ashland Global have also seen slowing sales over the last five quarters. Into the future, I believe they will not achieve the same level of sales growth as 2019, given this trend, which led me to forecast only 9.5 percent growth rate for the fiscal year 2020. I forecasted the long-term sales growth at 2 percent because the United States GDP is forecasted to be at 2 percent or below into the future. I performed a sensitivity analysis for the Hawkins stock price to change in sales growth and the weighted average cost of capital.

Current: \$ 38.64		WACC						
		6.7	7.0	7.3	7.6	7.9	8.2	8.4
Sales Growth	3.50%	49.26	46.00	43.05	40.37	37.92	35.68	34.30
	4.00%	51.19	47.67	44.48	41.59	38.96	36.55	35.06
	4.50%	53.32	49.50	46.05	42.93	40.09	37.50	35.90
	5.00%	55.65	51.51	47.78	44.40	41.34	38.55	36.83
	5.50%	58.21	53.72	49.67	46.02	42.71	39.71	37.85
	6.00%	61.01	56.14	51.75	47.80	44.22	40.98	38.98

I forecasted the cost of goods sold to sales rate to be slightly lower than the five-year average due to statements made by management in their most recent quarterly report stating that pricing in the commodities market has been stable and they have negotiated better pricing in their vendor contracts. I project selling, general and administrative expenses to be 11 percent in the future because this has been their consistent rate. They have continually made it a focus to keep these expenses at a minimum, and without an expected increase in the sales rate into the future, these expenses should remain constant. Depreciation over net property plant and equipment should stay constant into the future. I expect no changes to their level of debt. I forecast all other ratios to be the same as the most recent year.

## VALUATION AND INVESTMENT DECISION

To derive a valuation price of USD **33.79**, I used the corporate valuation model, which discounts expected free cash flows at the WACC. Hawkins released its most recent financial statements on May 23, 2019.

I also perform relative valuation using Innophos Holdings as the comparable company in the industry. There is a wide range of estimates of price per share using the different multiples below. The price/sales multiple and the market/book multiple yield the least extreme of the valuations, however both show different investment recommendations. The price/earnings ratio provides a price per share of \$80.44 because the earnings of Innophos are proportionally higher than Hawkins historical earnings. The same can be said of the EV/EBITDA multiple.

Multiples	IPHS Value	Hawkins PPS	Valuation	Investment Decision
Price/Sales	0.60	\$31.34	Overvalued	Sell
Price/Earnings	29.49	\$80.44	Undervalued	Buy
EV/EBITDA	2.67	\$13.59	Overvalued	Sell
Market/Book	1.86	\$51.16	Undervalued	Buy

\*IPHS ratios captured on November 24, 2019

In discounting the free cash flows at the WACC, I arrived at the price of UDS **33.79**, which is below the current price of USD 43.56. The intrinsic value I calculated is more than 10 percent

below the current market price, and more than one standard deviation from the mean return. Based on this observation, I will suggest a SELL recommendation for this security until economic or market conditions change.



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**Hawkins Inc (NMS: HWKN)***In Thousands of USD*

<b>Income Statement</b>	<b>04/02/2017</b>	<b>04/01/2018</b>	<b>03/31/2019</b>	<b>3/31/2020</b>	<b>3/31/2021</b>	<b>3/31/2022</b>	<b>3/31/2023</b>	<b>3/31/2024</b>
Sales	483,593	504,169	556,326	609,177	657,911	697,386	725,281	739,787
Costs of goods sold (COGS)	367,297	390,919	439,176	472,112	513,171	543,961	565,719	584,432
Sales, general and administrative expe	58,844	58,895	58,640	67,009	72,370	76,712	79,781	81,377
Depreciation	8,455	16,686	16,303	16,887	18,238	19,332	20,105	20,507
<b>Operating profit</b>	<b>48,997</b>	<b>37,669</b>	<b>42,207</b>	<b>53,169</b>	<b>54,133</b>	<b>57,381</b>	<b>59,676</b>	<b>53,471</b>
Interest expense	3,181	3,825	3,839	3,821	6,230	4,531	4,460	4,042
Interest income	-	-	-	-	-	-	-	-
Nonoperating income (Expense)	-	-	73	80	86	92	95	97
Earnings before taxes (EBT)	45,816	33,844	38,441	49,427	47,989	52,941	55,311	49,526
Tax expense	13,493	(5,899)	9,097	10,380	10,078	11,118	11,615	10,401
Net income before extraordinary items	32,323	39,743	29,344	39,047	37,912	41,823	43,696	39,126
After-tax extraordinary income (Expens	(168)	(39,116)	-	-	-	-	-	-
<b>Net income (NI)</b>	<b>32,155</b>	<b>627</b>	<b>29,344</b>	<b>39,047</b>	<b>37,912</b>	<b>41,823</b>	<b>43,696</b>	<b>39,126</b>
Dividends-- preferred	-	-	-	-	-	-	-	-
Dividends-- common	8,683	9,161	11,975	13,214	14,581	16,089	17,754	19,590
Additions to RE	23,472	(8,534)	17,369	25,834	23,331	25,734	25,942	19,536
<b>Balance Sheet</b>	<b>04/02/2017</b>	<b>04/01/2018</b>	<b>03/31/2019</b>	<b>3/31/2020</b>	<b>3/31/2021</b>	<b>3/31/2022</b>	<b>3/31/2023</b>	<b>3/31/2024</b>
<b>Assets</b>								
Cash	6,861	4,990	9,199	10,073	10,879	11,531	11,993	12,233
Inventory	52,735	65,322	65,526	71,751	77,491	82,141	85,426	87,135
Accounts receivable	57,298	63,507	63,966	70,043	75,646	80,185	83,392	85,060
Other short-term operating assets	5,511	6,749	5,762	6,309	6,814	7,223	7,512	7,662
Short-term investments	-	-	-	-	-	-	-	5,436
Total current assets	122,405	140,568	144,453	158,176	170,830	181,080	188,323	197,525
Net plant, property, & equipment (PPE)	121,540	123,826	118,628	129,898	140,289	148,707	154,655	157,748
Other long-term operating assets	196,994	157,878	157,878	215,892	186,707	197,909	205,825	209,942
Long-term investments	1,686	2,564	3,396	3,719	4,016	4,257	4,427	4,516
<b>Total assets</b>	<b>442,625</b>	<b>424,836</b>	<b>424,355</b>	<b>507,685</b>	<b>501,842</b>	<b>531,953</b>	<b>553,231</b>	<b>569,731</b>
<b>Liabilities and Equity</b>								
Accounts payable (AP)	29,756	33,424	29,314	32,099	34,667	36,747	38,217	38,981
Accruals	14,445	13,103	12,483	13,669	14,762	15,648	16,274	16,600
Other operating current liabilities	1,174	1,241	1,299	1,422	1,536	1,628	1,694	1,727
All short-term debt	7,989	9,864	9,907	65,065	31,098	26,914	16,434	9,833
Total current liabilities	53,364	57,632	53,003	112,255	82,064	80,937	72,618	67,140
Long-term debt	100,594	96,408	79,974	74,915	72,889	75,926	77,838	79,373
Deferred taxes	42,040	27,383	26,673	29,207	31,543	33,436	34,774	35,469
Preferred stock	-	-	-	-	-	-	-	-
Other long-term liabilities	4,758	7,321	8,088	8,856	9,565	10,139	10,544	10,755
Total liabilities	200,756	188,744	167,738	225,234	196,061	200,437	195,773	192,738
Par plus PIC Less treasury (and other	182,715	185,472	188,628	188,628	188,628	188,628	188,628	188,628
Retained earnings (RE)	59,154	50,620	67,989	93,823	117,153	142,887	168,830	188,365
Total common equity	241,869	236,092	256,617	282,451	305,781	331,515	357,458	376,993
<b>Total liabilities and equity</b>	<b>442,625</b>	<b>424,836</b>	<b>424,355</b>	<b>507,685</b>	<b>501,842</b>	<b>531,953</b>	<b>553,231</b>	<b>569,731</b>

**Page 2****Hawkins Inc (NMS: HWKN)***In Thousands of USD*

<b>Statement of Cash Flows</b>	<b>04/02/2017</b>	<b>04/01/2018</b>	<b>03/31/2019</b>	<b>3/31/2020</b>	<b>3/31/2021</b>	<b>3/31/2022</b>	<b>3/31/2023</b>	<b>3/31/2024</b>
<b>Operating Activities</b>								
Net income	32,155	627	29,344	39,047	37,912	41,823	43,696	39,126
Depreciation	8,455	16,686	16,303	16,887	18,238	19,332	20,105	20,507
Change in deferred tax	(202)	(14,657)	(710)	2,534	2,337	1,893	1,337	695
	-	-	-	-	-	-	-	-
Change in inventory	(878)	(12,587)	(204)	(6,225)	(5,740)	(4,649)	(3,286)	(1,709)
Change in accounts receivable	1,973	(6,209)	(459)	(6,077)	(5,603)	(4,539)	(3,207)	(1,668)
Change in other short-term operating assets	4,773	(1,238)	987	(547)	(505)	(409)	(289)	(150)
Change in accounts payable	(365)	3,668	(4,110)	2,785	2,568	2,080	1,470	764
Change in accruals	1,432	(1,342)	(620)	1,186	1,094	886	626	325
Change in other current liabilities	93	67	58	123	114	92	65	34
<b>Net cash from operating activities</b>	<b>47,436</b>	<b>(14,985)</b>	<b>40,589</b>	<b>49,713</b>	<b>50,413</b>	<b>56,509</b>	<b>60,517</b>	<b>57,926</b>
	-	-	-	-	-	-	-	-
<b>Investing Activities</b>								
Investment in PPE	(13,674)	(18,972)	(11,105)	(28,156)	(28,629)	(27,749)	(26,053)	(23,600)
Investment in other long-term operating assets	(6,033)	39,116	-	(58,014)	29,186	(11,202)	(7,916)	(4,117)
<b>Net cash from investing activities</b>	<b>(19,707)</b>	<b>20,144</b>	<b>(11,105)</b>	<b>(86,171)</b>	<b>556</b>	<b>(38,952)</b>	<b>(33,970)</b>	<b>(27,717)</b>
	-	-	-	-	-	-	-	-
<b>Financing Activities</b>								
Change in short-term investments	-	-	-	-	-	-	-	(5,436)
Change in long-term investments	538	(878)	(832)	(323)	(297)	(241)	(170)	(89)
Change in short-term debt	2,500	1,875	43	55,158	(33,967)	(4,185)	(10,480)	(6,601)
Change in long-term debt	(29,304)	(4,186)	(16,434)	(5,059)	(2,027)	3,037	1,912	1,536
Preferred dividends	-	-	-	-	-	-	-	-
Change in preferred stock	-	-	-	-	-	-	-	-
Change in other long-term liabilities	(8,914)	2,563	767	768	709	574	406	211
Change in common stock (Par + PIC)	2,981	2,757	3,156	-	-	-	-	-
Common dividends	(8,683)	(9,161)	(11,975)	(13,214)	(14,581)	(16,089)	(17,754)	(19,590)
<b>Net cash from financing activities</b>	<b>(40,882)</b>	<b>(7,030)</b>	<b>(25,275)</b>	<b>37,332</b>	<b>(50,163)</b>	<b>(16,904)</b>	<b>(26,086)</b>	<b>(29,969)</b>
	-	-	-	-	-	-	-	-
Net cash flow	(13,153)	(1,871)	4,209	874	806	653	461	240
Starting cash	20,014	6,861	4,990	9,199	10,073	10,879	11,531	11,993
<b>Ending cash</b>	<b>6,861</b>	<b>4,990</b>	<b>9,199</b>	<b>10,073</b>	<b>10,879</b>	<b>11,531</b>	<b>11,993</b>	<b>12,233</b>

**Page 3****Hawkins Inc (NMS: HWKN)**

<b>Ratios</b>	<b>2019</b>	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
<b>Productivity Ratios</b>					
Growth in sales	10.3%	4.3%	16.8%	13.7%	N/A
Receivables turnover	8.70	7.94	8.44	6.98	9.02
Inventory turnover	8.49	7.72	9.17	7.98	8.55
Operating working capital turnover	5.49	5.43	6.28	4.26	4.84
Net fixed asset turnover	1.57	1.40	1.52	1.35	3.02
Total asset turnover	1.11	1.00	1.09	0.92	1.41
Invested capital turnover	1.22	1.11	1.22	1.02	1.86
<b>Liquidity Ratios</b>					
Current ratio	2.73	2.44	2.29	2.85	3.96
Quick ratio	1.49	1.31	1.31	1.80	2.56
Cash ratio	0.17	0.09	0.13	0.40	1.10
Short-term investments over investe	-	-	-	-	0.07
Operating Cycle	84.96	93.27	83.05	97.98	83.14
Cash Cycle	65.73	69.07	60.59	71.42	63.01
<b>Financial Risk (Leverage) Ratios</b>					
Total debt-to-equity ratio	0.65	0.80	0.83	1.09	0.27
Total debt-to-equity ratio (excluding	0.55	0.68	0.66	0.90	0.21
Total financial debt-to-equity ratio	0.35	0.45	0.45	0.63	0.03
Interest coverage ratio (accounting)	10.99	9.85	15.40	26.78	72.94
Interest coverage ratio (cash-base)	15.24	14.21	18.06	33.46	89.30
Total debt-to-assets ratio	0.40	0.44	0.45	0.52	0.21
Total financial debt over total asset:	0.21	0.25	0.25	0.30	0.03
Long-term financial debt over inves	0.21	0.26	0.25	0.32	0.03
<b>Profitability/Valuation Ratios</b>					
Gross profit margin	21.06%	22.46%	24.05%	22.80%	23.17%
EBITDA margin	10.52%	10.78%	11.88%	11.07%	13.62%
Operating profit margin	7.59%	7.47%	10.13%	8.87%	11.12%
NOPAT margin	5.64%	5.44%	7.05%	12.92%	11.46%
Earnings before taxes margin	6.91%	6.71%	9.47%	8.54%	10.97%
Net margin	5.27%	0.12%	6.65%	5.58%	7.88%
Return on Assets	6.91%	0.15%	7.26%	5.13%	15.69%
Return on Equity	11.43%	0.27%	13.29%	10.73%	14.10%
Net investment rate	10.70%	179.98%	-26.31%	390.26%	469.21%
Dividend payout ratio	40.81%	1461.08%	27.00%	35.73%	27.40%
ROIC	8.38%	6.93%	8.43%	27.33%	N/A

**Hawkins Inc (NMS: HWKN)**

<b>Valuation</b>	<b>3/31/2020</b>	<b>3/31/2021</b>	<b>3/31/2022</b>	<b>3/31/2023</b>	<b>3/31/2024</b>	<b>3/31/2025</b>	<b>3/31/2026</b>	<b>3/31/2027</b>	<b>3/31/2028</b>	<b>3/31/2029</b>
FCFs	(34,375,792)	52,476,986	13,140,552	18,271,247	17,460,218	23,199,294	24,359,259	25,577,222	26,856,083	28,198,887
PV FCFs	40,767,144	(35,510,505)	694,633	4,423,793	8,118,933	11,677,502	10,801,014	10,462,089	10,133,799	9,815,811
Value of Operations	546,560,928	540,003,423	572,231,421	602,036,370	635,156,418	665,319,981	696,857,781	729,827,275	764,287,850	800,300,837
Value of Investments	3,718,620	4,071,889	4,397,640	4,705,475	4,987,803	5,237,193	5,499,053	5,774,006	6,062,706	6,365,841
Value of Firm	572,776,299	566,302,152	600,182,424	631,521,995	666,287,612	697,942,115	731,039,887	765,641,377	801,809,069	839,607,505
- Financial Debt	148,837,074	116,112,108	122,943,744	126,491,677	132,742,663	135,431,223	139,262,565	144,451,290	151,241,012	159,907,772
Implicit Value of Equity	423,939,225	450,190,044	477,238,680	505,030,319	533,544,949	562,510,892	591,777,322	621,190,087	650,568,057	679,699,733
Number of Shares Outstanding	10,654,887	10,654,887	10,654,887	10,654,887	10,654,887	10,654,887	10,654,887	10,654,887	10,654,887	10,654,887
Price per share	\$ 39.79	\$ 42.25	\$ 44.79	\$ 47.40	\$ 50.08	\$ 52.79	\$ 55.54	\$ 58.30	\$ 61.06	\$ 63.79