

# Huffy Corporation

NYSE: HUF - \$8.65

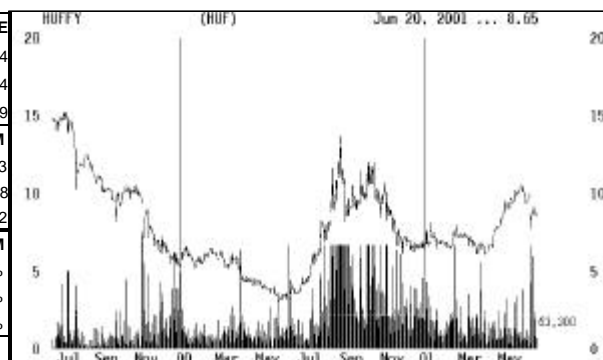
[www.huffy.com](http://www.huffy.com)

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## HUF Lowers Guidance Due to Weaker Than Expected Sales

Current Data		EPS		P/E	
Fiscal Year End	Dec	2000	\$ 1.03	8.4	
Current Price	\$ 8.65	2001E	\$ 0.53	16.4	
52-Week Range	14-3	2002E	\$ 0.87	9.9	
Shares Out (Mill)	10.2	<b>Valuation</b>		<b>Current</b>	<b>LTM</b>
Ave Volume LTM	86,577	P/E (Next FY)	16.37	7-3	
Market Cap. (Mill)	\$ 88.23	P/B	1.18	1.5-0.8	
LTD/Total Capital	0.0%	Price/Sales	0.18	0.21-0.12	
Institutional Holdings	37.0%	<b>Operating Data</b>		<b>1Q01</b>	<b>LTM</b>
Insider Holdings	9.3%	Sales Growth	-18.8%	13.1%	
Book Value	\$ 7.31	Operating Margin	2.0%	5.8%	
10Yr Bond	5.20%	Net Inc. Growth	188.7%	132.3%	

Source: Baseline except for EPS estimates, researchstock.com



Source: Baseline

### Key Investment Points

- Sales below original expectations due to weak retail sell-through and a reduction in a major service (Huffy Service First) project.
- HUF expects EPS for 2Q01 to be \$0.04-\$0.07 versus \$0.06 in 2Q00.
- FY guidance reduced to \$0.50-\$0.75 from \$1.00-\$1.10.
- Our revised 12-18 month target price is \$10.00.

### Company Description

Huffy Corporation ("HUF") designs and manufactures sport products and provides services for retailers. The Company's Consumer Products segment makes bicycles, basketball backboards, backboard support systems, goals and related products through its wholly-owned subsidiaries: Huffy Bicycle Company and Huffy Sports Company. The Company's Huffy Service First unit provides retailers with in-store and in-home assembly and repair and in-store display services for a variety of products.

## Weak Economy Reduced Sales: Management Lowered Earnings Forecast

While there were some isolated signs of strength during the start of the quarter, it apparently did not last. Management cited the current economic malaise as the major cause that adversely impacted the retail sector and caused a large client to pull a major service project. Management also noted that they do not expect to recoup the sales lost in 2Q01 and that sales for the rest of the year will be lower than they previously forecast.

Of the three main business segments, bikes and scooters remain the weakest link. Bike sales have slowed as consumers switched to lower price points and as retailers try to increase profits by minimizing inventories. The scooter market is saturated with low priced/low quality product that is clogging the pipeline. While HUF does not compete in the low-end market, we think price sensitive consumers are trading down, just as they are in bikes. Management noted that basketball systems (backboards) and Huffy Service First ("HSF") sales are expected to be relatively flat with last year.

**The stock was more resilient than we expected.** On June 12<sup>th</sup> (the first trading day after the announcement) the shares dropped from \$9.98 (the closing price on June 11<sup>th</sup>) to an intra day low of \$7.75. Most of the drop occurred at the outset and held steady to close at \$8.20. Since then, the shares have moved steadily upward. Normally, when a company announces a 50% decline in EPS expectations, the stock will drop by a like amount. In HUF's case, there are three possible explanations for the stock's reaction:

1. Most shareholders did not sell because they believe in the long-term value of HUF's brand name and cash flow potential while others saw a chance to get in at a low price,
2. The Market has become numb to news of this type, or
3. The Market did not care because it is unaware of HUF's story because it is an under followed stock.

Despite the recent price drop, HUF shares continue to outperform its peer group (companies with sales greater than \$500 million) on a longer-term basis (see Table 1)

(% Change)	3 Days	1 Wk	1 Mo	6 Mos	YTD	12 Mos.
<b>HUF</b>	<b>-3.7</b>	<b>0.0</b>	<b>-12.6</b>	<b>28.1</b>	<b>33.1</b>	<b>142.8</b>
BIKE	-2.3	-1.3	-5.3	5.8	5.8	-44.3
Sector Ave.	0.1	-1.2	3.8	34.9	36.6	6.2
Sales>\$500MM	1.4	-0.1	2.4	32.0	25.6	5.7

Source: Baseline, researchstock.com

## Outlook

We are reducing our EPS forecast to reflect our revised revenue expectations. Our current model is at the low end of Management's guidance because we think it could take longer than expected for the economy to correct.

We now expect sales to fall 28% in 2001 due to a difficult comparison with 2000's scooter enhanced results and weak results in 2001. We also lowered our 2002 sales growth assumption from 5% to 4%. As a result, our 2001 EPS forecast is now \$0.53 (the low end of management's guidance of \$0.50 - \$0.75) from \$1.07. Our 2002 estimate was reduced to \$0.87, versus our previous \$1.18. Tables 2 and 3 contain our revised outlook for annual and quarterly results.

<b>Table 2: Operating Forecast</b>						
(\$ Million, except per share)	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>
Revenues	580.7	584.2	422.9	488.2	<b>352.2</b>	<b>369.9</b>
Cost of Goods Sold	488.6	392.2	386.1	406.8	<b>298.5</b>	<b>310.7</b>
Gross Profit	92.1	76.2	36.7	81.3	<b>53.7</b>	<b>59.2</b>
SG&A	75.7	59.7	56.2	53.8	<b>44.2</b>	<b>44.0</b>
Plant Reconfig	0.0	21.3	38.6	0.7	<b>0.0</b>	<b>0.0</b>
Operating Income	16.4	-4.9	-58.0	26.9	<b>9.5</b>	<b>15.2</b>
Interest Expense/ (Inc.)	3.9	2.5	1.8	8.4	<b>1.1</b>	<b>1.0</b>
Other Income/Expenses	1.0	0.0	0.3	1.3	<b>-0.4</b>	<b>-0.4</b>
PreTax Income	11.5	-7.4	-60.1	17.1	<b>8.8</b>	<b>14.6</b>
Income Taxes	3.0	-2.9	-20.8	6.4	<b>3.4</b>	<b>5.5</b>
Discont. Ops	0.5	2.3	6.1	24.3	0.0	<b>0.0</b>
Net Income	9.0	-2.2	-33.3	35.0	<b>5.5</b>	<b>9.0</b>
<b>EPS-Diluted (as reported)</b>	<b>\$ 0.69</b>	<b>\$ (0.18)</b>	<b>\$ (3.13)</b>	<b>\$ 3.39</b>	<b>\$ 0.53</b>	<b>\$ 0.87</b>
From on-going operations				<b>\$ 1.03</b>	<b>\$ 0.53</b>	<b>\$ 0.87</b>
Diluted Shares	13.1	12.3	10.6	10.3	<b>10.4</b>	<b>10.4</b>
Effective Tax Rate	26%	39%	35%	38%	<b>38%</b>	<b>38%</b>
<b>Boldface data are forecasts.</b>						
<b>Growth Rates</b>						
Sales	0.2%	0.6%	-27.6%	15.4%	<b>-27.8%</b>	<b>5.0%</b>
Net Income	22.1%	-124.2%	-1437.6%	205.1%	<b>-84.3%</b>	<b>64.9%</b>
EPS					<b>-48.9%</b>	<b>64.9%</b>
<b>Margin Analysis</b>						
Gross	15.9%	13.0%	8.7%	16.7%	<b>15.3%</b>	<b>16.0%</b>
Operating	2.8%	-0.8%	-13.7%	5.5%	<b>2.7%</b>	<b>4.1%</b>
Net	1.5%	-0.4%	-7.9%	7.2%	<b>1.6%</b>	<b>2.4%</b>

<b>Table 3: Quarterly Operating Forecast</b>								
(\$ Million, except per share)	<b>1Q00</b>	<b>2Q00</b>	<b>3Q00</b>	<b>4Q00</b>	<b>1Q01</b>	<b>2Q01</b>	<b>3Q01</b>	<b>4Q01</b>
Revenues	100.07	122.03	123.88	142.21	81.24	<b>81.00</b>	<b>90.00</b>	<b>100.00</b>
Cost of Goods Sold	85.31	104.97	102.03	114.53	69.61	<b>70.07</b>	<b>75.15</b>	<b>83.70</b>
Gross Profit	14.76	17.06	21.84	27.68	11.64	<b>10.94</b>	<b>14.85</b>	<b>16.30</b>
SG&A	12.90	11.60	12.54	16.73	10.04	<b>10.05</b>	<b>12.00</b>	<b>12.10</b>
Plant Reconfig	1.72	1.61	-1.82	-0.80	0.00	<b>0.00</b>	<b>0.00</b>	<b>0.00</b>
Operating Income	0.15	3.85	11.12	11.74	1.59	<b>0.89</b>	<b>2.85</b>	<b>4.20</b>
Interest Expense/ (Inc.)	1.97	2.54	2.71	1.21	0.41	<b>0.20</b>	<b>0.30</b>	<b>0.20</b>
Other Expenses/ (Inc.)	-0.01	-0.12	1.36	0.11	-0.42	<b>0.00</b>	<b>0.00</b>	<b>0.00</b>
PreTax Income	-1.81	1.44	7.04	10.42	1.60	<b>0.69</b>	<b>2.55</b>	<b>4.00</b>
Income Taxes	-0.69	0.80	2.18	4.14	0.61	<b>0.26</b>	<b>0.97</b>	<b>1.52</b>
Net Income-Cont. Ops	-1.12	0.64	4.87	6.28	0.99	<b>0.42</b>	<b>1.58</b>	<b>2.48</b>
Discont. Ops.	-0.02	3.88	0.37	20.09	0.00	<b>0.00</b>	<b>0.00</b>	<b>0.00</b>
Net Income	-1.14	4.51	5.24	26.37	0.99	<b>0.42</b>	<b>1.58</b>	<b>2.48</b>
EPS-Diluted	\$ (0.11)	\$ 0.06	\$ 0.47	\$ 2.54	\$ 0.10	\$ <b>0.04</b>	\$ <b>0.15</b>	\$ <b>0.24</b>
From Cont. ops.	\$ (0.11)	\$ 0.06	\$ 0.50	\$ 0.61	\$ 0.10	\$ <b>0.04</b>	\$ <b>0.15</b>	\$ <b>0.24</b>
Diluted Shares	10.165	10.265	10.386	10.4	10.369	<b>10.369</b>	<b>10.369</b>	<b>10.369</b>
Effective Tax Rate	38%	56%	31%	40%	38%	<b>38%</b>	<b>38%</b>	<b>38%</b>
<b>Margin Analysis</b>								
Gross	14.8%	14.0%	17.6%	19.5%	14.3%	<b>13.5%</b>	<b>16.5%</b>	<b>16.3%</b>
EBITDAR	1.9%	4.5%	7.5%	7.7%	2.0%	<b>1.1%</b>	<b>3.2%</b>	<b>4.2%</b>
Operating	0.1%	3.2%	9.0%	8.3%	2.0%	<b>1.1%</b>	<b>3.2%</b>	<b>4.2%</b>
Net	-1.1%	3.7%	4.2%	18.5%	1.2%	<b>0.5%</b>	<b>1.8%</b>	<b>2.5%</b>
<b>Boldfaced data are estimates.</b>								

## Valuation

We lowered our 12-18 month target price to \$10.00 from \$13.00 based upon our revised EPS forecast and changed in our P/E assumptions to reflect our expectations of 20%+ EPS growth in 2002. As shown in Table 4, our revised range is \$12.61-\$5.60 versus our prior range of \$13.13-\$4.60. We chose a target price above the average to reflect our expectations of the upside potential.

<b>Table 4: Target Price Calculations</b>						
		<b>Multiples</b>			<b>2002</b>	<b>Target</b>
		<b>LTM</b>	<b>Current*</b>	<b>Forecast</b>	<b>Estimate</b>	<b>Range</b>
<b>Price/Book</b>	High	3.8	1.2	1.8	\$ 8.45	\$ 15.22
	Low	0.8		0.8		\$ 6.76
<b>Price/Sales</b>	High	0.34	0.17	0.33	\$ 35.67	\$ 11.77
	Low	0.07		0.10		\$ 3.57
<b>P/E*</b>	High	3.6	16.3	20.0	\$ 0.87	\$ 17.43
	Low	-4.9		10.0		\$ 8.72
* Current P/E is based on 2001 EPS forecast						
		Average	High		\$ 14.81	
			Low		\$ 6.35	
			Average		\$ 10.58	

We think this is a reasonable target because our multiple assumptions are, for the most part, based upon current levels (see Table 5).

	P/E		P/B	P/CF	P/Sales	Sales/ Share	Ent Val/ EBITDA
	2001	2002					
<b>HUF</b>	<b>16.4</b>	<b>9.9</b>	<b>1.2</b>	<b>4.0</b>	<b>0.17</b>	<b>\$50.24</b>	<b>1.7</b>
BIKE	-	-	0.5	604.1	0.20	\$19.59	8.6
Sector Ave.	25.5	33.1	2.2	30.1	1.21	\$18.61	16.0
Sales>\$500MM	26.2	49.8	2.8	12.7	0.97	\$32.80	10.4

Source: Baseline, researchstock.com

### **Risk Considerations**

In addition to normal investment risk, investors need to consider the following when evaluating an investment in the shares of this stock:

The shares are thinly traded and could experience significant volatility.

The Company is not widely followed by Wall Street analysts. As a consequence, any improvement in operations may not be reflected in the share price as quickly as it might if the Company was widely followed.

The EPA issue is a wild card. While the company has reserved an amount it deems adequate, it is possible that the Company could have a higher liability for any one of a number of reasons. The potential liability is discussed in detail in the notes to the financial statements in the SEC filings (10-Qs and 10-Ks).

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