07/28/2020: At Home, Inc. (HOME)

Business Description: At Home Group Inc. operates home decor superstores in the United States. The company's stores offer home furnishings, including accent furniture, furniture, mirrors, patio cushions, rugs, and wall art; and accent décor, such as artificial flowers and trees, bath, bedding, candles, garden and outdoor decor, holiday accessories, home organization, pillows, pottery, vases, and window treatments. - *TIKR.com*

Thesis: Short-term slowdowns in same-store sales and margins have given us an opportunity to purchase a fast-growing, competitively advantaged speciality retailer insulated from online and big box competitors. On a normalized basis, HOME is a growing, 10% EBIT margin company with a store model no retailer can match.

HOME's Advantages: Cliff Sosin of CAS Investment Partners laid out HOME's competitive advantages in his Q1 2020 letter. Echoing his sentiment, HOME relies on a few key advantages. First, they employ a Costco-like store model. 3-5 employees operate over 100K sqft of warehouse space in a bare-bones self-service atmosphere. Given their space, HOME can fill their store with *50K+* items. This allows the company to negotiate lower purchasing prices. And as the company expands stores, their purchasing power only increases. Like Costco, all cost savings flow through to the customer in the form of lower prices.

The second main advantage is (what Cliff calls) the "internet-ability" of HOME's transactions. Since HOME sells decor, furniture and fixtures, consumers opt for an in-person touch and feel experience before purchasing. Additionally, it costs a lot to ship HOME's product, making in-person pick-up an economically positive option. And even against companies that specifically cater to delivering furniture (Wayfair), HOME wins on cost ($70/order compared to Wayfair's $200-$300). On average, consumers save 20% shopping at HOME.

Store-Level Economics: Based on 2019 figures, the company generates roughly $6.5M in sales/store and $1.1M in EBITDA/store. They currently have 219 stores growing roughly 20%/year. These stores have an average payback period of ~2 years, with 2nd-generation real estate EBITDA margins close to 30%. Though growing 20%/year, HOME's only penetrated 37% of their total potential. That means in a perfect world HOME operates 590 stores throughout the US with 30% incremental store EBITDA margins.

Valuation: Let's assume HOME reaches 60% market penetration, equivalent to Home Goods today. That would get us 365 stores. Holding our above metrics constant that leaves us with $2.37B in revenue and $365M in EBITDA. We can also project operating income given their (normally) robust 10% operating margin. At $2.37B that's $237M in operating income (11% yield). Now, what if HOME reaches 75% penetration (442 stores). In that world we have a company generating $2.87B in revenue, $486M in EBITDA and $287M in operating income (14% yield).

Risks: There's a few risks with the thesis. First is debt. The company's aggressively reduced leverage from 5.2x to 3.3x. Between growing the number of stores and paying down debt, there will likely be little cash flow for shareholders in the short-term. There's also more nuanced risks like poor merchandise selection, competition from "shop online pickup in store" (HOME has its own BOPIS system) and poor weather impacting outdoor furniture sales. These all appear transitory, but we'll update accordingly.

Chart Analysis: At Home, Inc. (HOME)

The stock broke above its inverse head & shoulders neckline on strong volume last week and trades above its 50MA.

