

Arconic Inc.(ARNC)

\$16.40 (As of 03/30/20)

Price Target (6-12 Months): **\$18.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 03/09/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:B

Value: C

Growth: B

Momentum: D

Summary

Earnings estimates for Arconic for the first quarter and 2020 have been going down in the past month. The company is well placed to gain from strong demand trends in aerospace and North American automotive markets. Major contract wins in aerospace will support its financial performance. Also, the company will likely benefit from cost-cutting and productivity actions. However, Arconic faces challenges in the GRP unit. The segment faces headwinds from operational challenges in the aluminum extrusions business. Softness in the commercial transportation market is another worry, which is stemming from slowing growth in manufacturing and freight as well as lower new truck orders. The company may face some challenges due to the reduced production of the Boeing's 737 MAX. High balance sheet leverage is another concern.

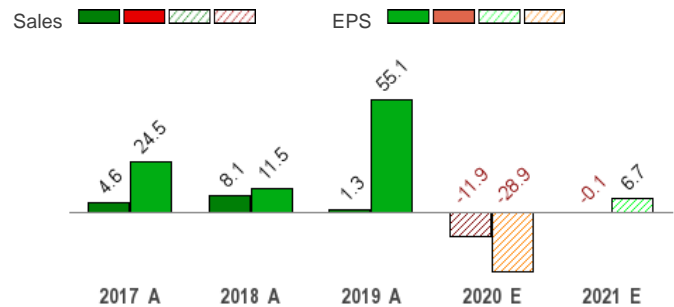
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$34.27 - \$11.38
20 Day Average Volume (sh)	6,069,037
Market Cap	\$7.1 B
YTD Price Change	-46.7%
Beta	1.47
Dividend / Div Yld	\$0.08 / 0.5%
Industry	Mining - Non Ferrous
Zacks Industry Rank	Top 37% (95 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-1.9%
Last Sales Surprise	-2.0%
EPS F1 Est- 4 week change	-34.5%
Expected Report Date	05/05/2020
Earnings ESP	0.0%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					12,496 E
2020	3,217 E	3,131 E	3,121 E	3,035 E	12,504 E
2019	3,541 A	3,691 A	3,559 A	3,401 A	14,192 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.34 E				\$1.60 E
2020	\$0.53 E	\$0.40 E	\$0.39 E	\$0.37 E	\$1.50 E
2019	\$0.43 A	\$0.58 A	\$0.58 A	\$0.53 A	\$2.11 A

*Quarterly figures may not add up to annual.

P/E TTM	7.7
P/E F1	10.9
PEG F1	NA
P/S TTM	0.5

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 03/30/2020. The reports text is as of 03/31/2020.

Overview

New York-based Arconic Inc., formed through the separation of aluminum giant Alcoa Inc., is a global leader in multi-material, precision engineered products and solutions for a variety of industries.

On Sep 29, 2016, board of Alcoa Inc. approved the completion of the company's planned separation into two independent, publicly-traded companies – Arconic Inc. and Alcoa Corporation. The separation was completed and became effective on Nov 1, 2016. Alcoa Inc. changed its name to Arconic Inc. on Oct 31, 2016.

Arconic, which operates in 18 countries, is a leader in lightweight metals engineering and manufacturing globally. The company generated revenues of \$14.2 billion in 2019.

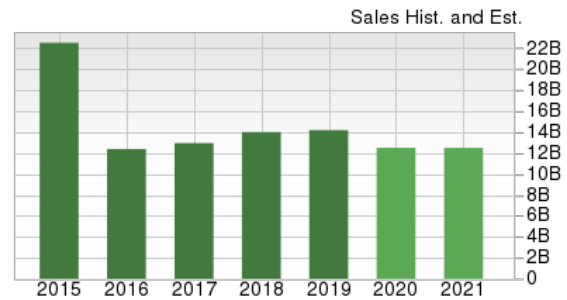
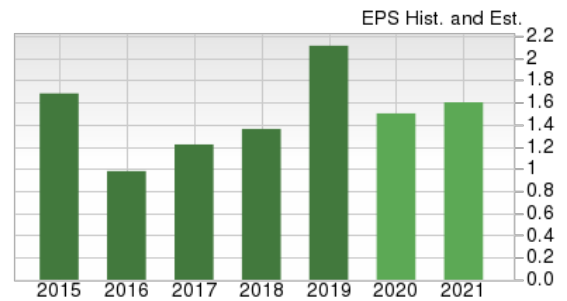
Arconic, in January 2019, announced that it is no longer pursuing a potential sale of the company as part of its strategy and portfolio review. The company is planning to separate its business into two public companies, which is expected to complete in the second quarter of 2020.

Arconic realigned its operations in third-quarter 2019 into two segments through the elimination of its Transportation and Construction Solutions segment and transfer of the Forged Wheels business to the Engineered Products and Forgings segment (earlier known as the Engineered Products and Solutions segment) and the Building and Construction Systems business to the Global Rolled Products segment.

Engineered Products and Forgings (EP&F) - This segment represents Arconic's fastening systems, engine products, engineered structures and forged wheels businesses. The segment accounted for around 50% of 2019 sales.

Global Rolled Products (GRP) - The segment represents global rolled products, aluminum extrusions and building and construction systems. The division caters to markets including industrial, commercial transportation, packaging and aerospace. The segment accounted for around 50% of sales.

Following the business separation, the EP&F businesses will remain in the existing company and will be renamed Howmet Aerospace Inc. at separation. The GRP businesses will be named Arconic Corporation. The company has targeted the separation to take effect on Apr 1, 2020.



Reasons To Buy:

▲ Arconic's shares have lost 16.6% over a year, outperforming the 39.5% decline recorded by its industry. Arconic is focusing on operational cost reduction and productivity improvements across its businesses, which should lend support to its bottom line. It is expected to continue to benefit from its cost-cutting actions. The company witnessed net cost reduction in the last reported quarter, which generated benefit worth \$76 million on a year-over-year basis. The company generated nearly \$213 million of year-over-year savings in 2019 led by cost reduction program. Also, operating cost reductions for 2019 were \$230 million, lower than its annual commitment of \$180 million. The company expects annual run rate operating costs to be reduced by \$300 million.

Arconic is well placed to gain from strong demand trends in aerospace and automotive markets. It should also benefit from its cost-cutting and productivity actions.

▲ Arconic is seeing strong demand in the aerospace market. It holds the number one market position in aluminum sheet and plate for the aerospace industry globally. Arconic expects growth in the aerospace market to be supported by strength in the commercial segment on higher air travel demand, new aircraft orders and strong order backlog. Arconic is seeing strong momentum in commercial aero engines and aero defense markets with double digit growth in organic revenues as witnessed in the last reported quarter. The company is investing \$100 million at its Whitehall and Morristown operations to meet the growing demand from aerospace engine customers. The Firth Rixson buyout has strongly placed Arconic to capture additional growth in aerospace through a broad spectrum of high-growth, value-add jet engine components. The purchase of RTI International has also broadened Arconic's titanium offerings and added advanced technologies and materials to its portfolio.

▲ Arconic is well positioned to capture the growing demand for aluminum sheet stemming from the transition of the North American auto industry to lightweighting. It is the market leader in providing aluminum sheet to the North American automotive market. The company leverages its breakthrough Micromill technology that manufacture the most advanced aluminum sheet on the market. The Micromill process produces an aluminum alloy that has 40% greater formability and 30% greater strength than the current automotive aluminum. Moreover, it continues to penetrate steel wheel market with aluminum wheels. The company's low-cost manufacturing wheels expansion in Hungary is fully-operational. This will enable Arconic to leverage its global footprint.

Reasons To Sell:

- ▼ Arconic faces certain challenges in its GRP unit. Revenues in the division declined 5% year over year in the last reported quarter and fell 2% year over year in 2019. Moreover, organic revenue growth was flat on a year-over-year basis. The segment faces headwind from operational challenges in the aluminum extrusions business. Softness in the commercial transportation market is another concern. The company expects commercial transportation to experience headwinds in 2020 due to slowing manufacturing and freight growth, higher current inventory levels as well as lower new truck orders.
- ▼ The company is expected to face some headwinds arising from the reduced production of the Boeing's 737 MAX. Arconic sells castings, forgings and advanced fasteners to Boeing as well as other aerospace suppliers. Boeing's decision to reduce production of 737 MAX may disrupt the aerospace supply chain in 2020 and hurt Arconic's margins.
- ▼ Arconic's high balance sheet leverage is another concern. The company is carrying essentially all of Alcoa Inc.'s debt following the business separation. While the company is taking actions to cut debt, it still has substantial total debt of roughly \$5.9 billion as against cash and cash equivalents of \$1.6 billion. Moreover, the company's long-term debt-to-equity ratio is 107.4%, which is higher than industry's average of 68.8%.

The company faces challenges in the GRP unit. High debt level is another concern. It also faces some headwinds due to the reduced production of Boeing's 737 MAX.

Last Earnings Report

Arconic Trails Earnings and Sales Estimates in Q4

Arconic recorded net income (as reported) of \$309 million or 70 cents per share in fourth-quarter 2019, up from \$218 million or 44 cents in the prior-year quarter.

Barring one-time items, adjusted earnings per share (EPS) came in at 53 cents. The figure trailed the Zacks Consensus Estimate of 54 cents.

Revenue fell 2% year over year to \$3,401 million and missed the Zacks Consensus Estimate of \$3,469 million.

Organic revenue inched up 1% year over year on the back of favorable product pricing and growth in the packaging, aerospace as well as industrial markets. However, this was significantly offset by softness in commercial transportation, automotive as well as building and construction markets.

2019 Highlights

In 2019, total revenue rose 1% year over year to \$14.2 billion and organic revenue rose 7%.

Net income came in at \$470 million or \$1.03 per share in 2019, down from \$642 million or \$1.30 per share in 2018.

Segment Highlights

EP&F: Revenue in the division totaled \$1.7 billion in the fourth quarter, up 1% year over year. Organic revenue in the segment rose 2%, supported by volume growth in aerospace that were partly offset by softness in commercial transportation.

GRP: Revenue in the division amounted to \$1.7 billion in the reported quarter, down 5% year over year. Organic revenue in the segment were flat on a year-over-year basis.

Financial Position

As of Dec 31, 2019, Arconic had cash and cash equivalents of \$1,648 million, down 27.6% year over year. Long-term debt fell 16.8% year over year to \$4,906 million.

Adjusted free cash flow in 2019 nearly doubled year over year to \$815 million from \$465 million.

Outlook

Arconic has issued guidance for full-year 2020.

The company expects sales in the range of \$13.9-\$14.2 billion. Adjusted EPS for 2020 is projected in the band \$2.22-\$2.42. Moreover, it expects adjusted free cash flow to be between \$800 million and \$900 million for 2020.

Arconic also expects adjusted EPS for first-quarter 2020 in the range of 47-53 cents.

Quarter Ending **12/2019**

Report Date	Jan 27, 2020
Sales Surprise	-1.96%
EPS Surprise	-1.85%
Quarterly EPS	0.53
Annual EPS (TTM)	2.12

Recent News

Arconic Announces Closure of Debt Offering Related to Separation – Feb 7, 2020

Arconic stated that its fully-owned subsidiary, Arconic Rolled Products Corporation (issuer), has closed the offering of \$600 million total principal amount of 6.125% second-lien notes due 2028.

Arconic Rolled Products plans to use the proceeds for making a payment to Arconic for funding the transfer of some of its assets to the issuer related to the company's plan to separate into two stand-alone, publicly traded companies. It also intends to use the proceeds for general corporate purposes.

Arconic Declares Debt Offering Related to its Separation – Jan 28, 2020

Arconic's fully-owned subsidiary, Arconic Rolled Products Corporation, has announced a proposed offering of second-lien notes. The terms of the notes and pricing are subject to market conditions.

Arconic Rolled Products plans to employ the proceeds from this proposed offering to make a payment to Arconic for funding the transfer of certain assets from the parent company to the issuer related to Arconic's plan to separate into two stand-alone, publicly traded companies as well as for general corporate purposes.

Valuation

Arconic's shares are down 16.6% over the trailing 12-month period. Stocks in the Zacks Mining - Non Ferrous industry and the Zacks Basic Materials sector are down 39.5% and 35.4% in the over the past year, respectively.

The S&P 500 index is down 11.8% in the past year.

The stock is currently trading at 6.88X forward 12-month earnings, which compares to 16.42X for the Zacks sub-industry, 9.93X for the Zacks sector and 17.02X for the S&P 500 index.

Over the past five years, the stock has traded as high as 26.66X and as low as 6.62X, with a 5-year median of 14.51X.

Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$18 price target reflects 7.56X forward 12-month earnings per share.

The table below shows summary valuation data for ARNC:

Valuation Multiples - ARNC					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	6.88	16.42	9.93	17.02
	5-Year High	26.66	27.42	21.12	19.34
	5-Year Low	6.62	11.12	9.82	15.18
	5-Year Median	14.51	15.26	13.51	17.42
EV/EBITDA TTM	Current	5.03	6.82	7.32	9.4
	5-Year High	8.84	17.18	18.22	12.88
	5-Year Low	4.04	4.49	6.56	8.27
	5-Year Median	6.17	8.96	10.56	10.78
P/B TTM	Current	1.56	0.98	1.39	3.42
	5-Year High	3.23	3.11	3.55	4.55
	5-Year Low	0.55	0.84	1.21	2.85
	5-Year Median	1.82	1.77	2.18	3.63

As of 03/30/2020

Industry Analysis Zacks Industry Rank: Top 37% (95 out of 254)



Top Peers

Mueller Industries, Inc. (MLI)	Outperform
Alcoa Corp. (AA)	Neutral
Allegheny Technologies Incorporated (ATI)	Neutral
Carpenter Technology Corporation (CRS)	Neutral
Constellium SE (CSTM)	Neutral
Haynes International, Inc. (HAYN)	Neutral
Kaiser Aluminum Corporation (KALU)	Neutral
Norsk Hydro ASA (NHYDY)	Underperform

Industry Comparison Industry: Mining - Non Ferrous				Industry Peers		
	ARNC Neutral	X Industry	S&P 500	ATI Neutral	CSTM Neutral	KALU Neutral
VGM Score	B	-	-	A	-	A
Market Cap	7.15 B	66.80 M	18.21 B	1.11 B	M	1.09 B
# of Analysts	1	2	13	4	3	1
Dividend Yield	0.49%	0.00%	2.3%	0.00%	%	3.89%
Value Score	C	-	-	A	C	C
Cash/Price	0.23	0.10	0.06	0.43	NA	0.32
EV/EBITDA	7.22	4.33	11.22	4.08	NA	8.16
PEG Ratio	NA	1.06	1.74	0.70	NA	NA
Price/Book (P/B)	1.55	0.66	2.41	0.50	NA	1.49
Price/Cash Flow (P/CF)	4.71	5.08	9.70	3.49	NA	6.79
P/E (F1)	10.76	16.18	15.12	10.54	NA	9.78
Price/Sales (P/S)	0.50	0.84	1.96	0.27	NA	0.72
Earnings Yield	9.15%	0.54%	6.55%	9.49%	NA%	10.23%
Debt/Equity	1.07	0.10	0.70	0.63	-25.41	0.71
Cash Flow (\$/share)	3.48	0.17	7.01	2.51	2.58	10.16
Growth Score	B	-	-	A	A	A
Hist. EPS Growth (3-5 yrs)	-6.23%	2.63%	10.89%	309.10%	4.03%	14.14%
Proj. EPS Growth (F1/F0)	-28.91%	-6.25%	1.80%	-31.40%	124.11%	2.92%
Curr. Cash Flow Growth	20.37%	-1.60%	5.93%	-13.16%	6.98%	4.60%
Hist. Cash Flow Growth (3-5 yrs)	-9.54%	7.87%	8.55%	13.25%	30.49%	8.82%
Current Ratio	1.42	1.23	1.23	2.71	1.06	4.58
Debt/Capital	51.50%	29.02%	42.57%	38.75%	NA	41.37%
Net Margin	3.31%	-1.40%	11.64%	6.25%	1.04%	4.07%
Return on Equity	20.28%	-0.03%	16.74%	7.63%	-54.43%	14.93%
Sales/Assets	0.80	0.44	0.54	0.74	1.37	1.04
Proj. Sales Growth (F1/F0)	-11.90%	0.00%	2.08%	-6.30%	-1.00%	-2.82%
Momentum Score	D	-	-	D	-	B
Daily Price Chg	-1.68%	0.00%	2.63%	-2.89%	NA%	1.38%
1 Week Price Chg	25.89%	12.32%	12.32%	44.16%	NA%	22.61%
4 Week Price Chg	-45.24%	-27.89%	-18.22%	-48.32%	NA%	-29.64%
12 Week Price Chg	-47.45%	-42.47%	-23.36%	-56.47%	NA	-37.10%
52 Week Price Chg	-16.58%	-50.69%	-17.22%	-66.98%	NA	-34.89%
20 Day Average Volume	6,069,037	60,675	4,211,236	3,697,713	0	178,713
(F1) EPS Est 1 week change	0.00%	0.00%	-0.19%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-34.50%	0.00%	-3.07%	0.97%	0.96%	0.00%
(F1) EPS Est 12 week change	-38.10%	-29.73%	-4.15%	-52.93%	-0.86%	-9.07%
(Q1) EPS Est Mthly Chg	-16.67%	-14.89%	-2.28%	0.00%	1.47%	0.00%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	C
Growth Score	B
Momentum Score	D
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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