Avnet, Inc. (AVT)

$19.79 (As of 03/18/20)

Price Target (6-12 Months): **$17.00**

|		
Long Term: 6-12 Months	**Zacks Recommendation:**	**Underperform**
	(Since: 01/28/20)	
	Prior Recommendation: Neutral	
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**4-Sell**
	Zacks Style Scores:	VGM:A
	Value: A Growth: B Momentum: D	

Summary

Weakness in the components industry due to macroeconomic headwinds are likely to keep affecting Avnet's overall performance in the near term. Downturn in Asia and soft manufacturing activities in Europe will hurt the company's industrial and automotive segments. Moreover, shorter lead times and lower average selling prices are likely to persist in the near term, creating pricing and margin pressures across Farnell business. Shares of the company have underperformed the industry in the past year. However, cost-saving efforts are significantly yielding. Strong performance in defense and aerospace and new opportunities in retail and healthcare are key positives. The industrial sector has started witnessing a rebound after a lull, which is an upside. Moreover, Avnet has been trying to expand presence in IoT, which is a lucrative industry.
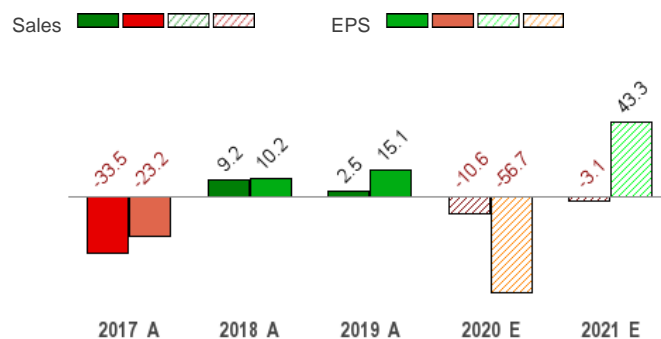
Price, Consensus & Surprise
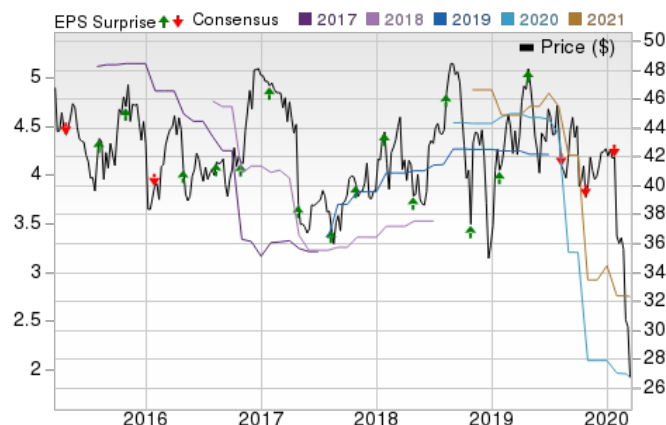
Data Overview

52 Week High-Low	**$49.03 - $17.85**
20 Day Average Volume (sh)	**1,264,033**
Market Cap	**$2.0 B**
YTD Price Change	**-53.4%**
Beta	**1.39**
Dividend / Div Yld	**$0.84 / 4.2%**
Industry	**Electronics - Parts Distribution**
Zacks Industry Rank	**Top 43% (110 out of 253)**
Last EPS Surprise	**-2.4%**
Last Sales Surprise	**2.3%**
EPS F1 Est- 4 week change	**-9.2%**
Expected Report Date	**04/23/2020**
Earnings ESP	**-17.0%**
P/E TTM	**6.5**
P/E F1	**11.1**
PEG F1	**0.8**
P/S TTM	**0.1**

Sales and EPS Growth Rates (Y/Y %)

Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	4,246 E	4,121 E	4,212 E	4,319 E	16,898 E
2020	4,630 A	4,535 A	4,099 E	4,180 E	17,444 E
2019	5,090 A	5,049 A	4,699 A	4,681 A	19,519 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	$0.52 E	$0.49 E	$0.74 E	$0.77 E	$2.55 E
2020	$0.60 A	$0.40 A	$0.37 E	$0.39 E	$1.78 E
2019	$1.03 A	$1.04 A	$1.09 A	$0.95 A	$4.11 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 03/18/2020. The reports text is as of 03/19/2020.

Overview

Based in Phoenix, AZ, Avnet Inc., (AVT) is one of the world's largest distributors of electronic components and computer products. The company's customer base includes original equipment manufacturers (OEMs), electronic manufacturing services (EMS) providers, original design manufacturers (ODMs), and value-added resellers (VARs). Avnet maintains an extensive inventory, including electronic products from more than 300 component and system manufacturers, which it distributes to customers worldwide.

Avnet distributes products for companies like International Business Machines Corp. and Hewlett-Packard Co. As part of its major restructuring initiative to focus on high growth businesses, the company sold its troubled TS business to Tech Data Corp. in a cash-stock deal worth $2.6 billion during fiscal 2017.

Avnet has two major operating segments — Electronic Components (EC) and Premier Farnell (PF). Through the EC segment, the company distributes semiconductors and Interconnect, passive and electromechanical devices (IP&E), and provides supply chain management, inventory replenishment system and non-complex engineering design services. This segment also offers integrated solutions, including technical design, integration and assembly of embedded products, systems and solutions for industrial applications.

EPS Hist. and Est.

Sales Hist. and Est.

Avnet's PF segment supports low volume customers that require electronic components quickly to develop and test their products. This segment provides a comprehensive suite of kits, tools, electronic components and industrial automation components to both engineers and entrepreneurs.

The company operates across the Americas; Europe, Middle East and Africa (EMEA); and Asia/Pacific (Asia) regions.

The product set consists of semiconductors (approximately 77% of fiscal 2019 revenues), Interconnect, IP&E (18%), and Others (2.5%). Region wise, Avnet generated approximately 26.3% of revenues from operations in the Americas in fiscal 2019 while EMEA contributed about 34.6%. Asia accounted for 39% of revenues.

Avnet's major competitors include Arrow Electronics Inc., Future Electronics, World Peace Group, Mouser Electronics and Digi-Key Electronics.
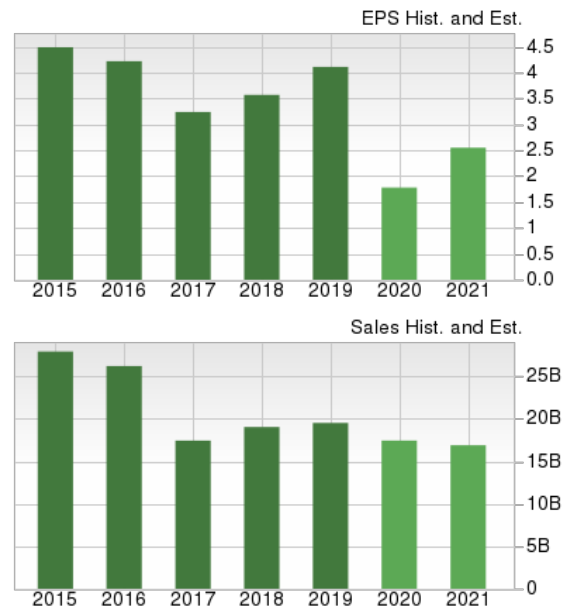
Reasons To Sell:

▼ Though the sale of the Technology Solution division to Tech Data Corporation has allowed Avnet to focus on high growth areas such as marketing electronic components and related products in the supply chain, it will take considerable time to reflect in the company's bottom line performances. This makes us cautious about the company's near-term prospects.

▼ Asia undoubtedly remains one of the largest growth drivers in the current environment. Although profitable in the long run, the company's extensive investments in the region will impact its margins in the near term. We also believe that any unfavorable currency fluctuations and an uncertain macroeconomic environment may temper growth at the company because of the major part of its revenues coming from outside the United States.

▼ Continued weakness in the industrial and automotive segments due to the downturn in China, overall slowdown in sales in Asia and headwinds from Europe, are affecting the company's growth. This makes us cautious about its near-term prospects.

▼ Avnet's domestic and foreign operations are subject to significant competition. It faces stiff competition from Arrow Electronics Inc. — a formidable rival. Arrow's acquisition of Waching's Wireless business, ALTIMATE Group, Global Link Technology, Redemtech and expansion in Sao Paulo, Brazil can turn out to be highly profitable, and pose a serious threat to Avnet, going forward.

Though the sale of the TS division will allow Avnet to focus on high growth areas in the supply chain, it will take considerable time to reflect in the company's bottom line performances.

Risks

- The recent forecast for worldwide IT spending by Gartner induced some optimism about Avnet's near-term performance. The research firm expects worldwide IT spending to grow 3.7% year over year in 2020, mainly driven by increased spending by companies in enterprise software. In its earlier report, Gartner had indicated that major technology trends, including Internet of Things (IoT), big data, artificial intelligence (AI) and blockchain, have been driving the overall IT spending. All this encourages us about the company's near-term prospects.

- In the past few months, Avnet has been taking major restructuring steps to streamline its business. It intends to focus on high growth businesses only and divest underperforming businesses. In doing so, the company sold its troubled Technology Solution business to Tech Data Corporation (TDC) for $2.6 billion during fiscal 2017. The divestment of the Technology Solution division has allowed Avnet to focus on high growth areas such as marketing electronic components and related products in the supply chain. The company intends to use its resources to make investments in embedded solutions, IoT and critical digital platforms as well as expand its footprint in newer markets.

- Over the last one year, Avnet has been trying to expand its presence in the IoT space. The company's acquisition of Dragon Innovation, a manufacturing consultancy and software vendor which enjoys strong presence in the IoT space, is considered to be in the same direction. Therefore, in our opinion, this acquisition will enable Avnet in providing powerful, simple-to-use tools to engineers which will enable them to manufacture and roll out hardware products in a more fast and cost-effective manner. On the IoT front, the company has made several partnerships with the likes of AT&T, as well as acquisitions, such as Premier Farnell and Hackster.io, to enhance its capabilities in this space. Per the company, the aforementioned acquisitions have expanded its "reach to more than two million customers and an active community of more than 750,000 entrepreneurs, makers and engineers."

- Acquisitions form an important part of the company's core strategy to bolster portfolio and expand global operations, while contributing significantly to the revenue stream. The acquisition of Dragon Innovation, a manufacturing consultancy and software vendor, helped the company expand presence in the IoT space. Avnet has also pursued a number of key acquisitions over the past few years, which are expected to comprehensively bolster its performance and augment its product base and operational network. This makes us optimistic about the company's growth prospects.

Last Earnings Report

Avnet's Q2 Earnings Miss, Revenues Beat Mark

Avnet recently reported second-quarter fiscal 2020 results wherein the bottom line missed estimates but the top line beat the same.

Its non-GAAP earnings were 40 cents per share, lagging the consensus estimate by 2.4%. The metric also plunged 61.5% year over year.

Revenues of $4.5 billion surpassed the Zacks Consensus Estimate by 2.3% but decreased 10% year over year. Nonetheless, the top line came within the company's guided range of $4.2-$4.6 billion.

Quarter Ending	12/2019
Report Date	Jan 23, 2020
Sales Surprise	2.34%
EPS Surprise	-2.44%
Quarterly EPS	0.40
Annual EPS (TTM)	3.04

Persistent weakness in the components industry due to macroeconomic woes hurt the top line. Softness in the industrial and automotive segments due to the downturn in Asia was further aggravated by the headwinds from Europe. Moreover, shorter lead times and lower average selling prices induced higher-than-expected pricing and margin pressures in the Farnell business, affecting the bottom line.

However, pricing stabilized as the quarter progressed. Strong performance in the vertical markets of defense and aerospace and new opportunities in retail and healthcare were positives. This industrial sector started to witness a rebound after a lull, which was an upside.

Quarter in Detail

Electronic Components segment fell 10.2% year over year to $4.2 billion due to the demand correction that began in December 2018.

Revenues from the Americas declined 8.8% year over year. However, revenues appear to be stabilizing, indicating that the downfall in the semiconductor space is bottoming out.

Revenues from the EMEA region were down 14.6%, particularly due to weakness in Europe.

Further, Asia revenues dipped 1.1% year over year due to macroeconomic issues. However, after a recent macroeconomic slowdown, revenues from Asia displayed stabilizing trends.

Purchasing Manager Index (PMI), which should exceed 50 to indicate industrial expansion, showed signs of stabilization in the United States and Asia toward the end of the quarter.

Premier Farnell segment's revenues of $331 million dropped 10.1% year over year. Nonetheless, the construction of a new Farnell distribution facility in Europe was a positive. SKU expansion is also making a steady progress, which is expected to boost this segment. Moreover, e-commerce global order penetration witnessed a significant increase.

During the quarter, Avnet completed the acquisition of software and embedded systems provider Witekio in a bid to expand and enhance its end-to-end IoT strategy. Witekio's solutions help developers address the challenges that crop up while developing IoT solutions. This is expected to add more capabilities in terms of embedded software, edge computing and security to Avnet's IoT business. The deal will also bolster Avnet's focus on simplifying the process of launching IoT products for client companies besides time and cost efficiently.

The company began to deploy PayPal in Europe, and WeChat Pay, Ali Pay and Union Pay in China to simplify business processes between Avnet and customers.

Avnet also saw lower revenues from Texas Instruments due to the ending of their 40-year distribution partnership in the previous reported quarter.

Margins

Avnet reported gross profit of $525.6 million, down 16.6% year over year. Gross margin shrank 90 basis points (bps) to 11.6%, primarily due to dwindling revenues and contracting margins in Farnell as well as global pricing pressures.

Adjusted operating income was $82.2 million, plunging 54% year over year. Adjusted operating margin came in at 1.8%, down 170 bps.

Adjusted operating expenses increased primarily due to a reserve for a potential bad debt from one customer.

However, focus on cost-reduction efforts was a boon, leading to $50 million in savings during the quarter.

Balance Sheet and Cash Flow

Avnet exited the fiscal second quarter with cash and cash equivalents of $488.8 million compared with $664.1 million recorded sequentially.

Long-term debt was $1.19 billion, same as the prior reported quarter.

The company returned $109 million to its shareholders in the form of $88 million as repurchased shares and $21 million worth of dividend.

Cash flow of $149 million was generated in the quarter.

Guidance

For third-quarter fiscal 2020, the company estimates sales in the range of $4.1-$4.5 billion with mid-point being $4.3 billion.

Non-GAAP earnings per share are estimated in the range of 38-48 cents with mid-point at 43 cents.

Market pressures are expected to persist in the near term. Avnet estimates operating margins at Farnell to lie below 10% in the forthcoming quarters.

Assuming modest improvement in the macro environment for both EMEA and Americas, management anticipates Electronic Components segment's operating margins between 2.2% and 2.5% by this summer.

Avnet expects to replace the Texas Instruments revenues with higher margin revenues by the end of fiscal 2022.

Recent News

On Feb 7, 2020, Avnet declared quarterly cash dividend 21 cents per share. Dividend will be payable on Mar 18 of shareholders record date as of Mar 4.

On Jan 7, 2020, Avnet launched a Partner Program at the CES 2020, which will aid IoT efforts by providing system integrators and OEMs with space to create IoT solutions cost effectively. Hence, the developers will be able to continue with their developments on the company's IoTConnect platform, which is powered by Microsoft's Azure IoT Suite.

On Nov 12, 2019, Avnet launched the low-cost, production-ready, qualified, single-board computer, MaaXBoard, which is based on the NXP i.MX 8M applications processor and ideal for embedded computing and applications that utilize AI at the edge.

On Sep 24, 2019, the company launched Avnet Super Store on Alibaba Group's China-focused B2B purchasing and wholesale marketplace, 1688.com.

On Sep 17, 2019, Avnet announced an agreement to acquire software and embedded systems firm, Witekio, to boost its IoT business.

On Sep 10, 2019, Avnet partnered with software company Trusted Objects to provide comprehensive industrial IoT (IIoT) solutions to customers with low-power IoT devices.

Valuation

Avnet's shares have lost 54.3% in the past six months, and 54.3% over the trailing 12 months. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector have fallen 41.2% and 10.1% in the past six months, respectively. Over the past year, the Zacks sub-industry has decreased 42.7%, while the sector plunged 7.6%.

The S&P 500 Index has declined 15.1% in the past six months and 11.4% in the past year.

The stock is currently trading at 7.88X forward 12-month earnings, which compares with 6.2X for the Zacks sub-industry, 16.38X for the Zacks sector and 14.12X for the S&P 500 Index.

Over the past five years, the stock has traded as high as 17.59X and as low as 7.57X, with a 5-year median of 10.05X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our $17 price target reflects 6.7X forward 12-months earnings.

The table below shows summary valuation data for AVT

Valuation Multiples - AVT		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	7.88	6.2	16.38	14.12
	5-Year High	17.59	12.3	22.01	19.34
	5-Year Low	7.57	6.2	16.36	14.12
	5-Year Median	10.05	9.66	19.3	17.42
EV/EBITDA TTM	Current	3.73	7.49	9.32	8.87
	5-Year High	9.54	9.22	12.84	12.88
	5-Year Low	3.73	5.09	7.6	8.31
	5-Year Median	6.22	7.258	10.8	10.78
EV/Sales TTM	Current	0.16	0.32	3.21	2.54
	5-Year High	0.44	0.42	4.45	3.46
	5-Year Low	0.16	0.24	2.54	2.14
	5-Year Median	0.3	0.32	3.53	2.82

As of 03/18/2020

Industry Analysis Zacks Industry Rank: Top 43% (110 out of 253)
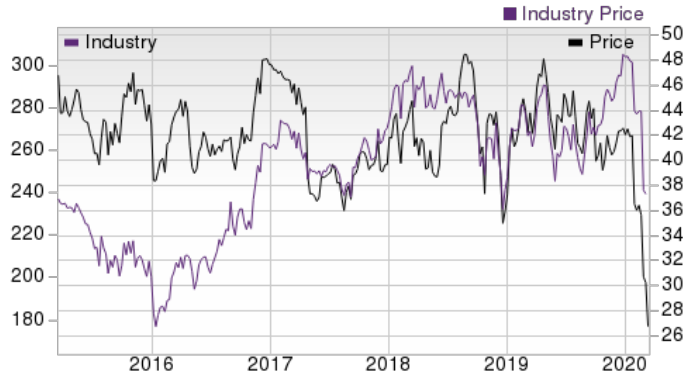
Top Peers

AMETEK, Inc. **(AME)**	**Neutral**
American Superconductor Corporation **(AMSC)**	**Neutral**
Advantest Corp. **(ATEYY)**	**Neutral**
KLA Corporation **(KLAC)**	**Neutral**
NVIDIA Corporation **(NVDA)**	**Neutral**
Tech Data Corporation **(TECD)**	**Neutral**
WESCO International, Inc. **(WCC)**	**Neutral**
Arrow Electronics, Inc. **(ARW)**	**Underperform**

Industry Comparison Industry: Electronics - Parts Distribution — Industry Peers

	AVT Underperform	X Industry	S&P 500	AME Neutral	ARW Underperform	TECD Neutral
VGM Score	A	-	-	B	A	B
Market Cap	1.98 B	1.32 B	16.02 B	15.04 B	3.31 B	3.54 B
# of Analysts	4	4	13	9	4	2
Dividend Yield	4.24%	0.00%	2.66%	1.10%	0.00%	0.00%
Value Score	A	-	-	D	B	B
Cash/Price	0.18	0.14	0.06	0.02	0.07	0.18
EV/EBITDA	4.21	4.76	10.21	12.15	17.51	5.58
PEG Ratio	0.86	1.07	1.46	1.75	1.22	NA
Price/Book (P/B)	0.50	0.50	2.18	2.93	0.69	1.14
Price/Cash Flow (P/CF)	2.65	3.86	8.79	12.55	3.86	5.79
P/E (F1)	12.07	7.72	12.92	15.43	5.80	7.56
Price/Sales (P/S)	0.11	0.11	1.74	2.92	0.11	0.10
Earnings Yield	8.99%	13.81%	7.70%	6.49%	17.24%	13.23%
Debt/Equity	0.36	0.54	0.70	0.44	0.54	0.43
Cash Flow ($/share)	7.46	7.46	7.01	5.23	10.65	17.27
Growth Score	B	-	-	A	A	C
Hist. EPS Growth (3-5 yrs)	-4.91%	5.55%	10.85%	11.36%	8.39%	23.42%
Proj. EPS Growth (F1/F0)	-56.69%	-2.13%	5.12%	1.57%	-6.23%	5.17%
Curr. Cash Flow Growth	-8.48%	-0.83%	6.03%	23.89%	-14.43%	-4.74%
Hist. Cash Flow Growth (3-5 yrs)	1.13%	1.86%	8.55%	10.17%	1.86%	18.72%
Current Ratio	2.38	2.34	1.23	1.42	1.52	1.23
Debt/Capital	26.66%	35.17%	42.57%	30.75%	35.17%	30.02%
Net Margin	0.55%	0.55%	11.57%	16.70%	-0.71%	1.01%
Return on Equity	7.86%	10.30%	16.74%	20.14%	12.67%	15.43%
Sales/Assets	2.11	1.78	0.54	0.56	1.78	2.94
Proj. Sales Growth (F1/F0)	-10.63%	0.00%	3.22%	1.54%	-6.82%	1.78%
Momentum Score	D	-	-	A	D	C
Daily Price Chg	-20.04%	-10.64%	-6.77%	-0.38%	-15.13%	-18.50%
1 Week Price Chg	-11.59%	-3.25%	-11.01%	-15.73%	-16.02%	-4.82%
4 Week Price Chg	-44.72%	-24.43%	-34.65%	-34.46%	-48.17%	-30.63%
12 Week Price Chg	-53.48%	-35.97%	-32.08%	-34.16%	-51.39%	-30.29%
52 Week Price Chg	-54.32%	-47.49%	-23.52%	-18.81%	-47.49%	-3.62%
20 Day Average Volume	1,264,033	792,483	3,834,688	2,580,108	804,432	1,292,752
(F1) EPS Est 1 week change	-7.05%	-4.10%	-0.06%	-1.57%	-4.87%	-0.23%
(F1) EPS Est 4 week change	-9.18%	-4.54%	-0.74%	-1.61%	-6.32%	0.38%
(F1) EPS Est 12 week change	-14.73%	-6.90%	-1.38%	-3.60%	-11.28%	0.38%
(Q1) EPS Est Mthly Chg	-16.48%	-4.75%	-0.85%	-1.25%	-8.40%	-2.47%

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	A
Growth Score	B
Momentum Score	D
VGM Score	A

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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