

BorgWarner Inc. (BWA)

\$35.35 (As of 07/06/20)

Price Target (6-12 Months): **\$37.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 06/11/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:A

Value: A

Growth: A

Momentum: C

Summary

BorgWarner's planned buyout of Delphi Technologies, expected to close in the second half of 2020, will further strengthen its propulsion leadership. The company's restructuring efforts, including footprint reduction in manufacturing technical centers and consolidation of Turbo/ETS business, bode well and are likely to help the firm to sustain margin profile and competitiveness in the long term. However, depressed demand of vehicles and weak consumer confidence amid COVID-19 are likely to impact the near-term earnings and sales of the firm. Unfavorable foreign currency translations are also likely to dent the results of BorgWarner. The company is bearing the brunt of higher research and development costs since the past several quarters and the trend is likely to continue. As such, investors are advised to wait for a better entry point.

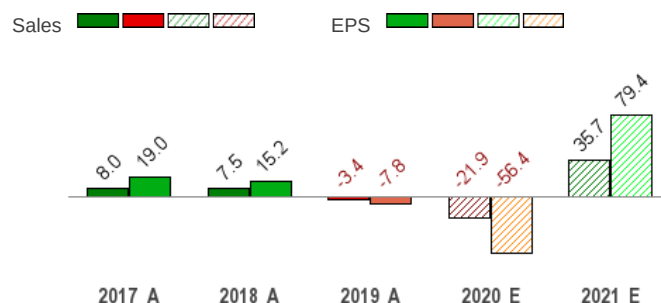
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$46.60 - \$17.00
20 Day Average Volume (sh)	2,930,683
Market Cap	\$7.3 B
YTD Price Change	-18.5%
Beta	1.74
Dividend / Div Yld	\$0.68 / 1.9%
Industry	Automotive - Original Equipment
Zacks Industry Rank	Top 27% (69 out of 251)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	57.1%
Last Sales Surprise	13.1%
EPS F1 Est- 4 week change	-0.4%
Expected Report Date	08/05/2020
Earnings ESP	46.0%
P/E TTM	9.1
P/E F1	19.6
PEG F1	2.5
P/S TTM	0.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	2,443 E	2,488 E	2,407 E	2,478 E	10,780 E
2020	2,279 A	1,141 E	2,104 E	2,373 E	7,944 E
2019	2,566 A	2,551 A	2,492 A	2,559 A	10,168 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.86 E	\$0.79 E	\$0.70 E	\$0.78 E	\$3.23 E
2020	\$0.77 A	-\$0.48 E	\$0.57 E	\$0.97 E	\$1.80 E
2019	\$1.00 A	\$1.00 A	\$0.96 A	\$1.17 A	\$4.13 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 07/06/2020. The reports text is as of 07/07/2020.

Overview

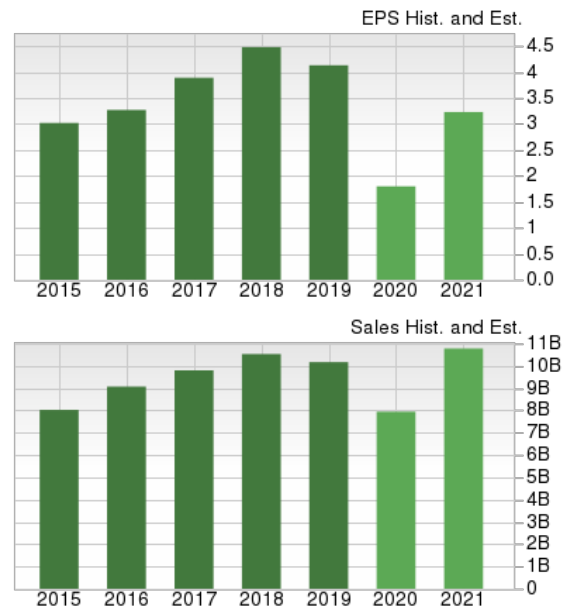
Michigan-based BorgWarner, Inc. is a global leader in clean and efficient technology solutions required for combustion, hybrid and electric vehicles. Its products include four-wheel-drive and all-wheel-drive transfer cases (primarily for light trucks and sport utility vehicles or SUVs), as well as automatic transmission and timing chain systems. These products are aimed at to improve vehicle performance, propulsion efficiency, stability and air quality. These products are produced and sold worldwide, primarily to OEMs of passenger cars, SUVs, trucks and commercial transportation products.

BorgWarner's largest customers include Volkswagen and Ford. The company operates manufacturing facilities catering to the customers in Europe, the Americas and Asia and is an original equipment supplier to every major automotive OEM in the world. The company's production and technical facilities are spread over 64 locations in 17 countries.

BorgWarner operates under two segments:

Engine segment (60.7% of sales in 2019): This segment develops and manufactures products to manage engines. Products include turbochargers, chains as well as emission and thermal systems. The segment also produces fluid pumps, including engine hydraulic pumps for variable cam timing and engine lubrication.

Drivetrain segment (39.3%): This segment engineers and manufactures components for automatic transmission and systems that combine such components. Products include friction plates, one-way clutches, transmission bands, torque converters and lock-up clutches for automatic transmission. The segment also offers polymer fans for engine cooling systems and sells products to OEMs of commercial trucks, buses as well as agricultural and off-highway vehicles, primarily in North America, South America, Europe and Asia.



Reasons To Buy:

- ▲ BorgWarner's planned buyout of Delphi Technologies will further strengthen its propulsion leadership. The combined company would offer flexibilities across the combustion, hybrid and electric propulsion lines, which is consistent with BorgWarner's evolution toward the future propulsion industry and transition toward electric vehicles. BorgWarner will also achieve cost synergies of approximately \$125 million by 2023 primarily by SG&A and procurement savings.
- ▲ As the global auto industry evolves to meet increasingly stringent emissions, BorgWarner is likely to benefit from accelerating vehicle electrification. In the long term, BorgWarner expects that hybrid and electric technologies will be the major revenue drivers. Electrification programs are likely to drive the company's backlog. Between 2020 and 2023, the backlog is expected to be \$2.5-\$2.63 billion. With a diverse product range, it projects that the new business gains will be more for its products that cater to hybrid and electric vehicles by 2023. Region wise, it expects 20% backlog in the Americas, 10% in Europe and 70% in Asia.
- ▲ The company's restructuring efforts, including footprint reduction in manufacturing technical centers and consolidation of Turbo/ETS business, bode well and is likely to help the firm to sustain margin profile and competitiveness in the long term. BorgWarner's turbocharger and timing products are its primary growth drivers. Since turbochargers help auto engines to remain in compliance with the tough emission standards, the demand for turbocharged engines is increasing. The timing system, which comes with one of the key technologies namely VCT, results in improved fuel economy and reduced emissions. High sales of turbocharger and timing products are likely to drive the top-line of the firm.
- ▲ The company fares well in the cash flow parameter. BorgWarner's FCF totaled \$700 million in 2019 and the company expects to generate \$675-\$725 million of FCFs in 2020. Full-year operating cash flow is expected to be approximately \$1,250 million, suggesting an uptick from \$1,008 million in 2019. BorgWarner's investor friendly moves also boost investors' confidence. In January 2020, the firm approved the implementation of a share-repurchase program of up to \$1 billion over the next three years.

BorgWarner's planned buyout of Delphi Technologies is likely to strengthen its propulsion unit.

Reasons To Sell:

- ▼ Coronavirus has rattled the auto sector with factory closure, low footfall in auto sales and supply-chain disruptions. Depressed demand of vehicles and weak consumer confidence amid COVID-19 are likely to impact the near-term earnings and sales of the automotive supplier. In fact, the company expects its second-quarter sales and earnings to take a severe hit from coronavirus woes.
- ▼ Bleak outlook for 2020 has dampened investors' sentiments. For full-year 2020, net sales are expected in the range of \$7.25-\$8 billion. This suggests a year-over-year decrease in organic sales of 20% to 27%. Full-year operating cash flow is expected to be in the range of \$530-\$780 million, down from the prior guidance of \$1,250 million. Free cash flow is expected to be in the range of \$100-\$300 million, down from the previous forecasted range of \$675-\$725 million.
- ▼ Unfavorable foreign currency translations are also likely to dent the results of BorgWarner. The company expects foreign currencies to result in a year-over-year decrease in sales of \$120 million, primarily due to the depreciation of the Euro, Chinese Renminbi and Korean Won against the U.S. dollar. The company is bearing the brunt of higher research and development costs since the past several quarters. The trend is likely to continue with the firm investing heavily in electrification-related programs. This is likely to mar its margins in 2020.
- ▼ BorgWarner expects a decline in light-vehicle production across all its major markets served, which is likely to dent its top line. The company expects the global vehicle markets to decline in the range of 25%-31% in 2020. The firm expects production in China, Europe and North America to decline around 18%-21%, 29%-38% and 27%-35%, respectively, on a year-over-year basis.

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Last Earnings Report

BorgWarner Delivers Weak Y/Y Results in Q1, Trims View

BorgWarner delivered adjusted earnings of 77 cents per share in first-quarter 2020, beating the Zacks Consensus Estimate of 49 cents. This was mainly aided by solid performance of the Engine segment. However, the reported figure came in lower than the year-ago quarter's \$1 per share. Net income amounted to \$129 million compared with the \$160 million reported in the prior-year quarter.

BorgWarner's net sales slid 11.2% year over year to \$2,279 million on unfavorable impact of foreign-currency fluctuations. The reported figure, however, beat the Zacks Consensus Estimate of \$2,014 million.

In the first quarter, operating income amounted to \$189 million compared with the prior-year quarter's \$264 million.

Segmental Performance

Net sales in the Engine segment fell to \$1,434 million from the year-ago quarter's \$1,598 million. The figure, however, surpassed the Zacks Consensus Estimate of \$1,411 million. Excluding impact of foreign-currency translation and divestiture of the thermostat product line, net sales were down 6.4% year over year and adjusted EBIT (earnings before interest, income taxes and non-controlling interest) dropped 11.3% to \$212 million chiefly on lower revenues.

In the Drivetrain segment, net sales decreased to \$860 million from the \$982 million reported in the prior-year quarter. The figure also missed the Zacks Consensus Estimate of \$891 million. Excluding the impact of foreign-currency translations, net sales declined 10.6%, year over year, and adjusted EBIT plunged 39% to \$63 million on lower revenues, and higher net research and development spending.

Financial Position

As of Mar 31, 2020, BorgWarner had \$901 million in cash compared with \$832 million as of Dec 31, 2019. In the first quarter, long-term debt was \$1,664 million, down from the \$1,674 million recorded at the end of 2019. The long-term debt-to-capital ratio stands at 25.4%.

Net cash provided by operating activities was \$263 million as of Mar 31, 2020, compared with \$40 million as of Dec 31, 2019. Investment in capital expenditure, including tooling outlays, remained unchanged at \$117 million in the March-end quarter.

Outlook

For full-year 2020, the company projects net sales of \$7.25-\$8 billion, down from the previous guidance of \$9.75-\$10.07 billion. Free cash flow is expected in the band of \$100-\$300 million in 2020, marking a decline from the prior guidance of \$675-\$725 million. Moreover, full-year operating cash flow is expected in the range of \$530 million to \$780 million.

Quarter Ending **03/2020**

Report Date	May 06, 2020
Sales Surprise	13.14%
EPS Surprise	57.14%
Quarterly EPS	0.77
Annual EPS (TTM)	3.90

Valuation

BorgWarner's shares are down 18.5% and 12.2% in the year-to-date period and over the trailing 12-month period, respectively. Stocks in the Zacks Automotive - Original Equipment industry and the Zacks Auto-Tires-Trucks sector are down 10.1% and up 13.1%, respectively, on a year to date basis. Over the past year, the Zacks sub-industry and sector are down 6% and up 26.6%, respectively.

The S&P 500 index is down 2.7% and up 5.7% in the year-to-date period and over the past year.

The stock is currently trading at 13.94X forward 12-month earnings, which compares to 24.35X for the Zacks sub-industry, 27.02X for the Zacks sector and 22.72X for the S&P 500 index.

Over the past five years, the stock has traded as high as 15.44X and as low as 4.86X, with a 5-year median of 10.48X.

Our Neutral recommendation indicates that the stock will in line with the market. Our \$37 price target reflects 14.62X forward 12-month earnings per share.

The table below shows summary valuation data for BWA:

Valuation Multiples - BWA					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	13.94	24.35	27.02	22.72
	5-Year High	15.44	24.35	27.02	22.72
	5-Year Low	4.86	8.52	8.23	15.15
	5-Year Median	10.48	11.48	9.7	17.42
EV/EBITDA TTM	Current	4.72	5.64	9.47	11.71
	5-Year High	10.26	8.32	11.2	12.81
	5-Year Low	2.73	4.45	6.93	8.24
	5-Year Median	6.6	6.35	9.16	10.75
P/S F12M	Current	0.78	0.67	0.84	3.54
	5-Year High	1.45	0.81	0.84	3.54
	5-Year Low	0.4	0.49	0.5	2.54
	5-Year Median	0.84	0.64	0.61	3.01

As of 07/06/2020

Industry Analysis Zacks Industry Rank: Top 27% (69 out of 251)



Top Peers

Company (Ticker)	Rec	Rank
Autoliv, Inc. (ALV)	Neutral	3
American AxleManufacturing Holdings, Inc. (AXL)	Neutral	3
Caterpillar Inc. (CAT)	Neutral	3
Dana Incorporated (DAN)	Neutral	3
DeereCompany (DE)	Neutral	3
Navistar International Corporation (NAV)	Neutral	3
PACCAR Inc. (PCAR)	Neutral	3
Tenneco Inc. (TEN)	Neutral	3

Industry Comparison Industry: Automotive - Original Equipment				Industry Peers		
	BWA	X Industry	S&P 500	CAT	DE	NAV
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	4	-	-	3	3	3
VGM Score	A	-	-	A	B	D
Market Cap	7.33 B	742.87 M	22.04 B	70.05 B	50.13 B	2.87 B
# of Analysts	9	3	14	10	9	4
Dividend Yield	1.92%	0.00%	1.89%	3.18%	1.90%	0.00%
Value Score	A	-	-	B	B	B
Cash/Price	0.12	0.19	0.07	0.10	0.19	0.57
EV/EBITDA	4.60	5.34	12.81	7.55	9.89	7.79
PEG Ratio	2.51	2.15	2.94	2.03	3.77	NA
Price/Book (P/B)	1.50	1.29	3.01	4.92	4.22	NA
Price/Cash Flow (P/CF)	5.65	4.40	11.87	8.04	9.69	4.51
P/E (F1)	19.46	26.92	21.54	24.37	26.37	NA
Price/Sales (P/S)	0.74	0.37	2.35	1.37	1.36	0.30
Earnings Yield	5.09%	2.28%	4.39%	4.10%	3.79%	-3.01%
Debt/Equity	0.34	0.42	0.76	1.71	2.89	-1.26
Cash Flow (\$/share)	6.26	2.94	6.94	16.10	16.53	6.40
Growth Score	A	-	-	B	B	F
Hist. EPS Growth (3-5 yrs)	9.34%	8.02%	10.90%	30.62%	17.88%	93.61%
Proj. EPS Growth (F1/F0)	-56.44%	-55.01%	-9.51%	-51.97%	-38.87%	-120.35%
Curr. Cash Flow Growth	-5.66%	-5.66%	5.51%	-6.65%	4.09%	9.70%
Hist. Cash Flow Growth (3-5 yrs)	3.79%	4.57%	8.55%	4.31%	3.09%	81.17%
Current Ratio	1.76	1.65	1.30	1.42	2.20	1.69
Debt/Capital	25.49%	38.35%	44.46%	63.12%	74.31%	NA
Net Margin	7.24%	1.62%	10.62%	10.41%	7.62%	1.92%
Return on Equity	17.15%	12.25%	15.75%	37.15%	23.01%	-5.82%
Sales/Assets	1.00	1.26	0.55	0.65	0.50	1.42
Proj. Sales Growth (F1/F0)	-21.87%	-13.60%	-2.57%	-23.27%	-19.33%	-34.59%
Momentum Score	C	-	-	A	D	D
Daily Price Chg	0.45%	1.47%	1.12%	1.34%	1.47%	2.34%
1 Week Price Chg	5.90%	3.42%	3.66%	4.35%	5.94%	1.73%
4 Week Price Chg	-5.78%	-8.56%	-7.12%	-6.02%	-5.09%	-2.43%
12 Week Price Chg	35.13%	27.26%	11.84%	13.40%	14.61%	52.59%
52 Week Price Chg	-12.20%	-13.83%	-6.03%	-4.01%	-2.24%	-13.17%
20 Day Average Volume	2,930,683	242,926	2,400,079	3,517,305	1,403,063	635,005
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	7.51%	0.72%	0.00%
(F1) EPS Est 4 week change	-0.37%	0.00%	0.00%	7.51%	0.72%	-0.45%
(F1) EPS Est 12 week change	-46.02%	-43.15%	-8.26%	-26.25%	-13.23%	-134.21%
(Q1) EPS Est Mthly Chg	3.65%	0.00%	0.00%	2.23%	-1.23%	-3.23%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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	A
Momentum Score	C
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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