

Cabot Corporation(CBT)

\$39.47 (As of 08/10/20)

Price Target (6-12 Months): **\$33.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 08/07/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:A

Value: B

Growth: A

Momentum: B

Summary

Cabot slipped to a loss in the third quarter of fiscal 2020. Adjusted loss and sales also missed the respective Zacks Consensus Estimate. The company is facing certain operational headwinds in the Performance Chemicals unit. Higher fixed costs in the Performance Chemicals unit is also likely to exert pressure on margins in the fiscal fourth quarter. Intense competition and weak demand are affecting prices in its metal oxides business. Softer demand and declining automotive production are other concerns. Lower volumes in the company's Reinforcement Materials segment is another headwind. Weak automotive production due to the coronavirus outbreak is affecting the company's volumes. Lower demand due to tire and automotive customer shutdowns in Europe and the Americas is also hurting volumes. High debt level is another concern.

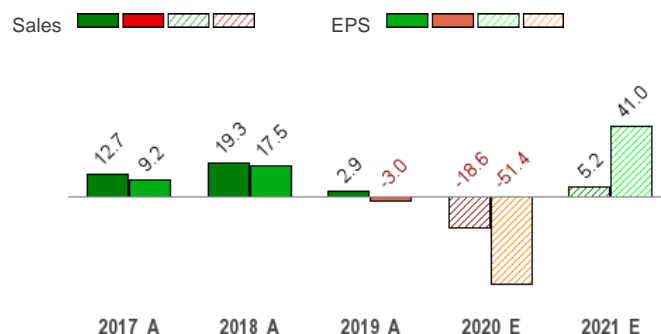
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$50.58 - \$20.00
20 Day Average Volume (sh)	205,183
Market Cap	\$2.2 B
YTD Price Change	-16.9%
Beta	1.71
Dividend / Div Yld	\$1.40 / 3.5%
Industry	<u>Chemical - Diversified</u>
Zacks Industry Rank	Bottom 21% (200 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-800.0%
Last Sales Surprise	-12.2%
EPS F1 Est- 4 week change	-3.6%
Expected Report Date	11/02/2020
Earnings ESP	1.3%
P/E TTM	16.2
P/E F1	20.8
PEG F1	2.1
P/S TTM	0.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					2,858 E
2020	727 A	710 A	518 A	694 E	2,716 E
2019	821 A	844 A	845 A	827 A	3,337 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$2.68 E
2020	\$0.69 A	\$0.77 A	-\$0.07 A	\$0.46 E	\$1.90 E
2019	\$0.87 A	\$0.99 A	\$1.00 A	\$1.05 A	\$3.91 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 08/10/2020. The reports text is as of 08/11/2020.

Overview

Boston, MA-based Cabot Corporation is a leading global specialty chemicals and performance materials company. The company offer a broad range of products and solutions to customers in every corner of the planet, catering to major industries such as transportation, infrastructure, environment and consumer. Its major products include rubber and specialty grade carbon blacks, specialty compounds, activated carbons, fumed metal oxides, inkjet colorants, aerogel and cesium formate drilling fluids.

Cabot operates through four segments – Reinforcement Materials, Performance Chemicals, Purification Solutions and Specialty Fluids. The company generated total sales of \$3,337 million in fiscal 2019, up 2.9% year over year.

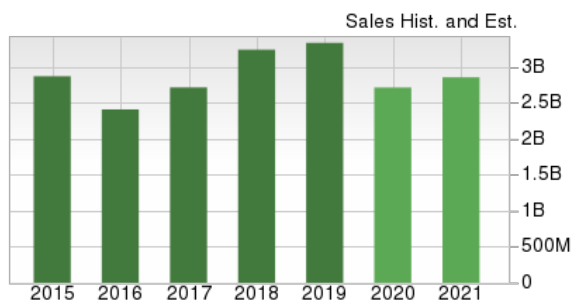
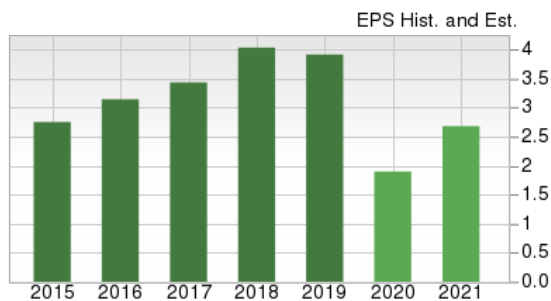
Reinforcement Materials (57% of Fiscal 2019 Sales): The segment makes rubber grade carbon blacks as well as compounds of carbon black and rubber using the company's patented elastomer composites manufacturing process.

Performance Chemicals (33%): The segment is comprised of specialty carbons and formulations business and metal oxides business. The specialty carbons and formulations business makes and markets specialty grades of carbon black, specialty compounds and inkjet colorants. The metal oxides business makes and markets fumed silica, fumed alumina and aerogel.

Purification Solutions (9%): The segment makes activated carbons that are used to remove contaminants from liquids and gases using a process called adsorption. These materials are used for the purification of water, air, food & beverages, pharmaceuticals and other liquids and gases.

Specialty Fluids (1%): The division makes a host of cesium products that include cesium formate brines and other fine cesium chemicals that are used in a range of industries and applications.

In June 2019, the company successfully closed the divestiture of its Specialty Fluids business to Sinomine (Hong Kong) Rare Metals Resources Co. Limited for \$135 million. The transaction enables the company to focus on growth opportunities in core businesses and execute the 'Advancing the Core' strategy.



Reasons To Sell:

- ▼ The company is witnessing certain operational headwinds in the Performance Chemicals unit. Cabot faces headwind from a challenging operating environment, especially in China. The company saw pricing weakness in the metal oxides business in the last reported quarter due to intense competition, which affected results in the Performance Chemicals unit. Net sales in the segment declined 12% year over year while profitability plunged 43%. For the unit, the company anticipates the challenging pricing environment to continue moving ahead. Cabot expects the business environment to remain challenging in the foreseeable future. Higher fixed costs in the Performance Chemicals unit is also likely to exert pressure on margins in the fiscal fourth quarter. Cabot expects the coronavirus pandemic to hurt volumes in fiscal 2020 in Europe and the Americas due to soft demand in the automotive market.
- ▼ Lower volumes across all regions hurt the company's Reinforcement Materials segment in the last reported quarter. In particular, coronavirus-induced shutdowns led to a 42% year-over-year decline in global volumes for this unit, which significantly impacted demand in the fiscal third quarter. Overall sales in the segment fell around 57% and the segment slipped to losses. The company expects lower volumes due to the pandemic to hurt margins in this segment in the fiscal fourth quarter. It expects volumes to be down 15% year over year in the unit in the fiscal fourth quarter. As such, lower volumes and margins in the segment is a concern.
- ▼ Weak automotive demand globally remains a concern, which may continue to impact the company's volumes. In the last reported quarter, automotive production was particularly soft in Europe and the Americas. Lower demand due to tire and automotive customer shutdowns in Europe and the Americas amid the coronavirus significantly hurt volumes in the fiscal third quarter. Volumes in the Americas were down 59% and the same in Europe was down 51% in the last reported quarter. As such, softer demand and declining automotive production remain a worry in fiscal 2020.
- ▼ Cabot's high debt level is also a concern. At the end of the fiscal third quarter, its long-term debt was at a high level of \$1,164 million, up 14.5% year over year. Further, its time-interest-earned ratio of 3.1 at the end of the fiscal third quarter fell from 4.4 in the prior quarter and has also deteriorated over the last few quarters. The company's low cash balance coupled with a weak revenue stream (as reflected by falling revenues over the past few quarters), may affect its ability to meet its debt obligations.

Cabot faces operational headwinds in the Performance Chemicals. Weak automotive demand globally may also continue to impact volumes. High debt level is also a matter of concern.

Risks

- Cabot remains committed to boost its specialty compounds business globally. The buyout of Tech Blend and commissioning of a new production line at its manufacturing facility in Belgium will help the company expand its global footprint in black masterbatch and compounds. It will also help beef up manufacturing capacity to better serve customers globally and grow in advanced polymeric materials. The company now has a complete range of black masterbatches from five manufacturing locations throughout Europe, Middle East, Asia and North America. The company expects the conductive carbon additives market, which is currently valued between \$350 million and \$400 million, to grow 20% over the next five years.
 - Cabot's buyout of the NSCC carbon plant in China will support growth of specialty carbons and formulations business. This acquisition will support its growth objectives and broaden capabilities as the company convert a 50,000 metric ton plant to support specialty carbons product lines. These investments will keep helping the company in meeting the growing demand for rubber and specialty carbons products. Moreover, the acquisition of a newly-commissioned CNT plant in China provides additional upside. The company expects that the plant has sufficient capacity to support growth over the next several years. The acquisition of Shenzhen Sanshun Nano New Materials has also strengthened the company's market position and formulation capabilities in the high-growth batteries market, especially in China. It is also expected to boost Cabot's global leadership position in carbon additives.
 - The company is likely to gain from higher volumes in the Purification Solutions unit. The segment's profitability improved both sequentially and on year-over-year basis in the last reported quarter. The upside was driven by higher margins from improved pricing and product mix and specialty applications as well as lower fixed costs. Going forward, the company is expected to see seasonally higher volumes stemming from some recovery from the coronavirus pandemic that will likely support margins.
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Last Earnings Report

Cabot Misses Earnings and Sales Estimates in Q3

Cabot slipped to a loss of \$6 million or 12 cents per share in the third quarter of fiscal 2020 (ended Jun 30, 2020) from a profit of \$32 million or 55 cents per share in the year-ago quarter.

Barring one-time items, adjusted loss per share was 7 cents in the reported quarter against adjusted earnings of a penny per share in the year-ago quarter. Also, the figure trailed the Zacks Consensus Estimate of a penny.

Net sales fell 38.7% year over year to \$518 million in the quarter. It also lagged the Zacks Consensus Estimate of \$589.9 million.

Quarter Ending 06/2020

Report Date	Aug 06, 2020
Sales Surprise	-12.20%
EPS Surprise	-800.00%
Quarterly EPS	-0.07
Annual EPS (TTM)	2.44

Segment Highlights

Reinforcement Materials' sales fell 57.3% year over year to \$197 million in the reported quarter. Earnings before interest and tax (EBIT) in the segment were at a loss of \$5 million against earnings of \$72 million in the year-ago quarter.

Sales in Performance Chemicals unit went down 12.4% year over year to \$220 million in the reported quarter. EBIT fell 43.2% year over year to \$21 million mainly due to lower volumes stemming from the coronavirus pandemic, an unfavorable product mix in specialty carbons as well as competitive pricing environment in the fumed metal oxides product line.

Sales in Purification Solutions declined 13.7% year over year to \$63 million in the quarter. EBIT rose 100% year over year to \$2 million on higher margins from better pricing and lower fixed costs.

Financial Position

Cabot had cash and cash equivalents of \$162 million at the end of the fiscal third quarter, down 10.2% year over year. The company's long-term debt rose 14.5% year over year to \$1,164 million.

Cash flow from operating activities was \$149 million in the reported quarter, up 29.6% year over year.

Outlook

Cabot expects volume and EBIT to improve significantly in the fiscal fourth quarter compared with fiscal third-quarter levels on the back of higher demand on improving economic outlook and recovery in automotive and replacement tire markets.

The company expects a substantial sequential improvement in demand in Reinforcement Materials as customer facilities resume in Europe and the Americas. In Performance Chemicals, it expects a modest improvement in volumes and product mix, which is likely to be offset by higher fixed costs.

Recent News

Cabot Completes Placement of Air Emission Control Equipment

Cabot, on **Jun 26, 2020**, announced a significant achievement in its project at Franklin, LA site in the United States. Management stated that the company received all its major emission control equipment and positioned the same for completion site as of Jun 2020.

Notably, Cabot is the first carbon black manufacturer to partner with the U.S. Environmental Protection Agency (EPA) in conjunction with the national enforcement initiative of EPA to control air emissions from carbon black producing facilities.

Good news is that the project already completed 90% of the estimated person-hours needed and is on track to finish ahead of schedule, that is, before the industry's April 2021 EPA deadline. Per management, the company has been steadily advancing despite the problems posed by Hurricane Barry in 2019 and coronavirus in 2020. Moreover, it is leveraging its extensive expertise in applying the best-in-class pollution control technologies to ensure that proven technologies are successfully implemented in Louisiana.

Cabot is expected to reduce NOx emissions by 90% using selective catalytic control and SO2 emissions by 95% through the use of wet gas scrubbing at its Franklin site. Notably, these systems are expected to lower annual NOx and SO2 footprint by roughly 900 and 6,500 tons a year, respectively, at its Franklin site.

Cabot Amends Credit Facilities to Increase Flexibility

Cabot, on **Jun 8, 2020**, announced that its revolving credit facilities were amended to increase the maximum leverage ratio permitted under the agreements.

The company's maximum leverage ratio, applicable on the last day of each fiscal quarter, will increase to 4.5 times from 3.5 times for the term of the credit facilities. Notably, the increase will start with the quarter ending Sep 30, 2020, and continue through the quarter ending Jun 30, 2021.

Reportedly, there were no changes in material terms under the agreements. Moreover, the agreements are slated to mature in October 2022.

Per management, increasing the maximum leverage ratio is a prudent step in offering incremental headroom due to the demand uncertainties stemming from the coronavirus pandemic. Notably, the move is expected to provide additional flexibility beyond the coronavirus outbreak-related stress-test scenarios, which the company has evaluated.

Moreover, Cabot is confident enough to generate an anticipated strong cash flow in the second half of the fiscal year. Also, the company expects its strong balance sheet to allow it to successfully navigate through this period of uncertainty.

Valuation

Cabot's shares are down 16.7% in the year-to-date period and up 3.6% over the trailing 12-month period. Stocks in the Zacks Chemical - Diversified industry and Zacks Basic Materials sector are down 9.3% and 0.1% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are up 0.7% and 10.4%, respectively.

The S&P 500 index is up 3.9% in the year-to-date period and up 16.3% in the past year.

The stock is currently trading at 15.11X forward 12-month earnings, which compares to 18.98X for the Zacks sub-industry, 15.2X for the Zacks sector and 22.75X for the S&P 500 index.

Over the past five years, the stock has traded as high as 17.67X and as low as 5.51X, with a 5-year median of 13.36X.

Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$33 price target reflects 12.93X forward 12-month earnings per share.

The table below shows summary valuation data for CBT:

Valuation Multiples - CBT					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	15.11	18.98	15.2	22.75
	5-Year High	17.67	18.98	21.06	22.75
	5-Year Low	5.51	8.97	9.86	15.25
	5-Year Median	13.36	13.15	13.53	17.58
EV/EBITDA TTM	Current	8.54	8.27	10.94	12.62
	5-Year High	50.13	13.12	18.08	12.84
	5-Year Low	3.73	5.24	6.56	8.25
	5-Year Median	8.43	7.48	10.77	10.9
P/B TTM	Current	2.14	1.72	2.43	4.67
	5-Year High	3.22	2.82	3.07	4.67
	5-Year Low	1.04	0.87	1.23	2.85
	5-Year Median	2.25	1.71	2.2	3.74

As of 08/10/2020

Industry Analysis Zacks Industry Rank: Bottom 21% (200 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Ashland Global Holdings Inc. (ASH)	Outperform	1
Axalta Coating Systems Ltd. (AXTA)	Neutral	3
Ferro Corporation (FOE)	Neutral	3
W.R. GraceCo. (GRA)	Neutral	3
Ingevity Corporation (NGVT)	Neutral	3
Orion Engineered Carbons S.A (OEC)	Neutral	2
Tronox Limited (TROX)	Neutral	3
Olin Corporation (OLN)	Underperform	5

Industry Comparison Industry: Chemical - Diversified				Industry Peers		
	CBT	X Industry	S&P 500	FOE	OEC	OLN
Zacks Recommendation (Long Term)	Underperform	-	-	Neutral	Neutral	Underperform
Zacks Rank (Short Term)	4	-	-	3	2	5
VGM Score	A	-	-	D	A	C
Market Cap	2.23 B	2.50 B	23.56 B	1.11 B	751.85 M	1.78 B
# of Analysts	6	3	14	4	3	4
Dividend Yield	3.55%	1.87%	1.71%	0.00%	4.83%	7.09%
Value Score	B	-	-	C	A	B
Cash/Price	0.07	0.13	0.07	0.06	0.22	0.14
EV/EBITDA	6.99	8.08	13.39	15.08	4.98	6.99
PEG Ratio	2.17	3.22	2.92	2.04	NA	NA
Price/Book (P/B)	2.14	1.81	3.18	3.07	4.99	0.81
Price/Cash Flow (P/CF)	6.00	6.83	12.69	8.82	3.51	2.59
P/E (F1)	21.67	20.29	22.16	19.21	16.57	NA
Price/Sales (P/S)	0.80	0.90	2.55	1.04	0.61	0.32
Earnings Yield	4.81%	4.64%	4.33%	5.20%	6.03%	-12.22%
Debt/Equity	1.12	0.60	0.77	2.28	4.15	1.86
Cash Flow (\$/share)	6.58	3.41	6.94	1.52	3.55	4.35
Growth Score	A	-	-	D	B	C
Hist. EPS Growth (3-5 yrs)	5.99%	8.03%	10.41%	6.47%	10.89%	11.74%
Proj. EPS Growth (F1/F0)	-51.49%	-24.36%	-6.51%	-15.66%	-59.89%	-329.17%
Curr. Cash Flow Growth	-22.87%	-9.82%	5.26%	-31.22%	-8.95%	-22.35%
Hist. Cash Flow Growth (3-5 yrs)	-2.25%	6.32%	8.55%	6.77%	11.92%	22.28%
Current Ratio	1.99	1.89	1.34	2.47	1.52	1.75
Debt/Capital	52.74%	37.80%	44.59%	69.47%	80.58%	65.05%
Net Margin	2.41%	3.83%	10.13%	-0.73%	3.53%	-4.14%
Return on Equity	12.99%	10.94%	14.59%	19.96%	43.99%	-4.60%
Sales/Assets	0.91	0.75	0.51	0.60	0.97	0.62
Proj. Sales Growth (F1/F0)	-18.61%	-7.20%	-1.54%	-33.48%	-23.42%	-9.67%
Momentum Score	B	-	-	C	C	C
Daily Price Chg	2.33%	0.98%	0.91%	4.83%	5.97%	2.64%
1 Week Price Chg	5.73%	4.02%	2.30%	9.75%	15.00%	-2.14%
4 Week Price Chg	6.94%	6.94%	8.54%	17.67%	15.41%	1.44%
12 Week Price Chg	20.52%	20.52%	13.68%	14.66%	49.94%	-5.29%
52 Week Price Chg	3.60%	3.08%	3.71%	15.35%	0.65%	-33.12%
20 Day Average Volume	205,183	53,995	2,015,804	315,832	323,895	2,087,153
(F1) EPS Est 1 week change	-1.90%	0.00%	0.00%	0.72%	12.50%	-15.74%
(F1) EPS Est 4 week change	-3.56%	0.00%	1.67%	0.72%	12.50%	-15.94%
(F1) EPS Est 12 week change	-9.51%	-0.92%	2.27%	0.00%	-2.17%	-6.59%
(Q1) EPS Est Mthly Chg	9.95%	3.13%	0.67%	-4.65%	33.33%	-78.57%

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	B
Growth Score	A
Momentum Score	B
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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