

Eaton Corporation plc (ETN)

\$88.24 (As of 07/02/20)

Price Target (6-12 Months): **\$93.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/29/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: B

Growth: C

Momentum: B

Summary

Eaton's wide market reach, R&D investments and spin-off of less profitable businesses are boosting operations. The company has taken measures to combat the economic crisis and decline in demand caused by the COVID-19 pandemic. Eaton's acquisition of Power Distribution is in sync with long-term growth objectives. Strong cash flow generation is supporting its shareholder friendly moves. Shares of Eaton have outperformed the industry in the past 12 months. However, Eaton's world-wide operations expose it to negative currency translation, cyber-attacks and security breaches, all of which might impact operations. Choppy end-market conditions and COVID-19-induced weakness have compelled the company to withdraw its 2020 earnings guidance.

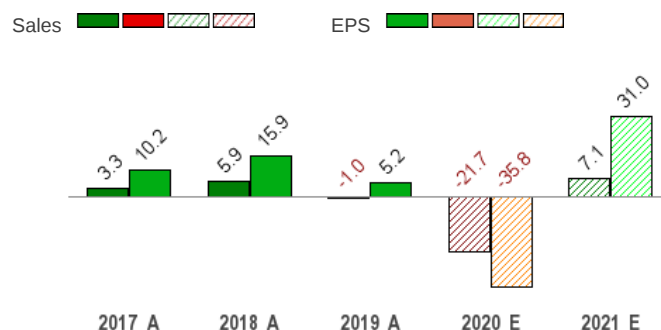
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$105.78 - \$56.42
20 Day Average Volume (sh)	2,489,501
Market Cap	\$35.3 B
YTD Price Change	-6.8%
Beta	1.14
Dividend / Div Yld	\$2.92 / 3.3%
Industry	Manufacturing - Electronics
Zacks Industry Rank	Top 33% (83 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	2.8%
Last Sales Surprise	-0.1%
EPS F1 Est- 4 week change	0.1%
Expected Report Date	08/04/2020
Earnings ESP	-11.8%
P/E TTM	16.0
P/E F1	24.2
PEG F1	2.8
P/S TTM	1.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,382 E	4,183 E	4,487 E	4,618 E	17,929 E
2020	4,789 A	3,672 E	3,999 E	4,311 E	16,742 E
2019	5,305 A	5,533 A	5,314 A	5,238 A	21,390 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.00 E	\$1.05 E	\$1.35 E	\$1.46 E	\$4.77 E
2020	\$1.09 A	\$0.51 E	\$0.90 E	\$1.13 E	\$3.64 E
2019	\$1.26 A	\$1.53 A	\$1.52 A	\$1.37 A	\$5.67 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 07/02/2020. The reports text is as of 07/03/2020.

Overview

Dublin, Ireland-based Eaton Corporation plc is a diversified power management company, and a global technology leader in electrical components and systems. It sells products in more than 175 countries and has 99,000 employees in 59 countries. The company was founded in 1916.

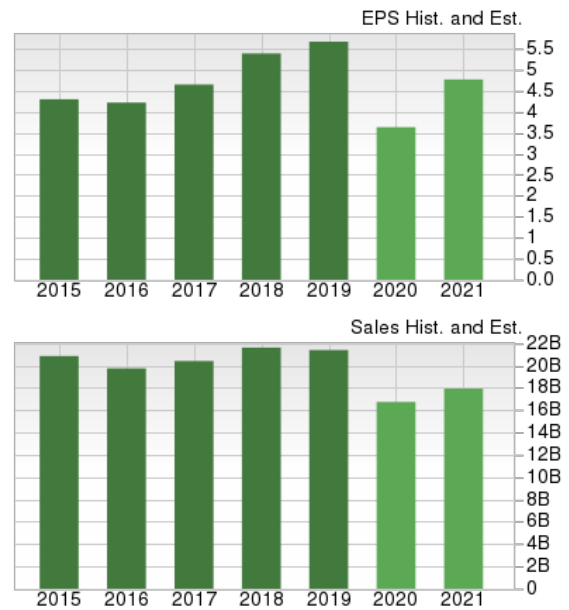
During first-quarter 2020, Eaton re-segmented certain reportable segments due to a reorganization of businesses. The new reportable segments are Electrical Americas and Electrical Global, which include Legacy Electrical Products and Electrical Systems and Services segments. The Filtration and Golf Grip businesses previously included in the Hydraulics segment and electrical aerospace connectors business, which was earlier under the Electrical Products segment, have been added to the Aerospace reportable segment, as part of the reorganization. Post reorganization, Eaton's reportable segments are **Electrical Americas**, **Electrical Global**, **Hydraulics**, **Aerospace**, **Vehicle** and **eMobility**.

The Electrical Americas segment includes sales contracts that are primarily for electrical and industrial components, power distribution and assemblies, residential products, single and three-phase power quality, wiring devices, circuit protection, utility power distribution, power reliability equipment, as well as services that are primarily produced and sold in North and South America. The Electrical Global segment consists of the same activities as mentioned in Electrical Americas but are primarily produced and sold outside of North and South America.

Vehicle segment includes the company's erstwhile truck and automotive segments. The truck segment designs, manufactures and markets powertrain systems and other components for commercial vehicle markets. Aerospace segment is a supplier of aerospace fuel, hydraulics and pneumatic systems for commercial and military use.

The eMobility segment focus on two technologies within electrical vehicles, namely Power electronics & conversion and Power distribution & circuit protection.

Eaton's segments — Electrical Americas, Electrical Global, Hydraulics, Aerospace, Vehicle and eMobility — contributed 37.3%, 23.9%, 10.6%, 14.2%, 12.5% and 1.5%, respectively, to first-quarter 2020 revenues.



Reasons To Buy:

- ▲ Eaton has been investing consistently in its R&D programs to introduce new products, including power management solutions which will reduce energy consumption and carbon emissions. The company has been upgrading the existing systems to maintain its strong position in global markets. In 2019, the company's R&D expenses amounted to \$606 million, up 3.8% from 2018. In the first quarter, R&D expenses were \$153 million compared with \$159 million in the year-ago period. In the first quarter, orders in Electrical Americas were up 3% year over year. The company continues to churn out new products aiming to facilitate effective and easy power management. Eaton's strategy to manufacture in the zone of sale has helped to offset the impact of tariff on material prices. The products supplied by the company have been deemed to be critical part of the global infrastructure and are absolutely essential in the crisis situation.

Eaton's wide market reach, acquisitions, spin-off of less profitable business, strong cash flow generation, share buybacks and product innovation are likely to drive its performance.

It activated and stood up its pandemic management and response team early, created a COVID-19 playbook, as well as kept most of the manufacturing units operational across the globe, in compliance with safety measures. The company trimmed the salaries of senior executives, eliminated merit increases in 2020, reduced discretionary spending, and implemented travelling and hiring freezes to lower costs and preserve liquidity amid this economic crisis as a result of the novel coronavirus. In the past 12 months, shares of Eaton have gained 7.2% compared with the industry's gain of 3.1%.

- ▲ Eaton operates in a number of markets and faces a wide array of competitors in varied niches. The quality of products supplied by the company enables it to retain a strong market position. In addition, Eaton's strategic acquisitions allow it to foray into new markets and enhance its revenue stream. Eaton supplies its products to around 175 countries and most importantly, this in a sense provides stability to the revenue generation ability of the company, as the loss of a customer will not have any significant impact on revenues and margins. Moreover, a diversified product portfolio offering energy efficient solutions helps to serve a wide customer base.
- ▲ The company made accretive acquisitions like Power Distribution and sold the less profitable lighting business for \$1.4 billion during the first quarter. It also entered into an agreement to sell the Hydraulics business for \$3.3 billion in cash. These divestitures will allow Eaton to focus on higher-margin core businesses. Contribution from acquired assets boosted total revenues by 2%, while the divested assets negatively impacted the same by 3.5% in the first quarter.
- ▲ Eaton continues to generate a stable cash inflow through proficient handling of operating activities. In 2019, The company's operating cash flow and free cash flow was \$3.5 billion and \$2.9 billion, respectively. It expects 2020 free cash flow in the range of \$2.3-\$2.7 billion. In addition to utilizing funds for growth ventures and several other activities, a strong cash generating capacity supports the company's systematic debt-reduction initiatives and shareholder-friendly moves.

The company utilized the proceeds from the Lighting business sale to repurchase shares worth \$1.3 billion during the first quarter, which will have a positive impact on earnings and increase the value of shareholders. The proceeds from the Hydraulics business divestiture will open opportunities for more share buybacks and strategic acquisitions. It paid dividend worth \$291 million in the first quarter of 2020 and its free cash flow generating capability will support shareholder-friendly moves.

- ▲ At first quarter-end, Eaton's total debt to capital was 37.1%, up from 34.2% at the end of fourth-quarter 2019, as the company repurchased shares worth \$1.3 billion in the quarter. It exited the first quarter with a long-term debt of \$8,176 million, up marginally from \$8,150 million at 2019-end. Eaton is trying to lower debts from the balance sheet. At first quarter-end, the company's cash and short-term investments were \$415 million, while short-term debt was \$337 million. It indicates that the company has enough liquidity to meet near-term obligation.

The times interest earned ratio of Eaton at first quarter-end was 13.4, up from 12 at the end of fourth-quarter 2019. The improving times interest earned ratio clearly indicates that the company will be able to fulfill debt obligations in the near term without any hassle. At a time when every entity is looking forward to preserve liquidity amid uncertainty as a result of the COVID-19 outbreak, Eaton's improving times interest earned ratio is reassuring for investors.

Reasons To Sell:

- ▼ Eaton operates in nearly 175 countries and has manufacturing facilities worldwide. This definitely enhances the revenue stream of the company but at the same time exposes it to disruptions like natural disaster, labor strike, war, political unrest, terrorist activity and economic upheaval. Such disturbances could delay shipments, stop production process and result in cancellation of orders. The outbreak of COVID-19 is also resulting in demand weakness in some of the end markets served.

Due to the prevailing economic uncertainty across the globe as a result of the COVID-19 pandemic, the company has decided to withdraw its full-year 2020 guidance. The company is expecting decremental margins of 25-30% for the full year owing to the pandemic.

- ▼ To conduct its business in an efficient manner, the company depends on its information technology network. These technology networks and systems may be susceptible to damage, disruptions or shutdowns due to failures during the process of upgrading or replacing software, databases or components; power outages; hardware failures; or computer viruses. In addition, cyber-attacks and security breaches could impact the operations of the company affecting its financial performance.
- ▼ Eaton utilizes a variety of raw materials and components in its businesses and has to depend on others for the supply of raw materials. So, any significant shortage, price increase, or supplier insolvencies could increase operating costs and adversely impact Eaton's competitive position.

Widespread operation exposes it to geo-political risks. Weakness in some end markets served and shortage of raw materials can impact the company's performance.

Last Earnings Report

Eaton's Q1 Earnings Beat Estimates, Revenues Miss

Eaton Corporation reported first-quarter 2020 earnings of \$1.09 per share, which surpassed the Zacks Consensus Estimate of \$1.06 by 2.8%. However, the reported earnings fell short of management's guided range of \$1.16-\$1.26 per share. The company's earnings were negatively impacted by 14 cents due to the COVID-19 pandemic impact.

GAAP earnings in the reported quarter were \$1.07 per share compared with \$1.23 in the year-ago period. The difference between GAAP and operating earnings in the reported quarter was due to a one-time charge of 2 cents associated with acquisitions and divestitures.

Quarter Ending **03/2020**

Report Date	Apr 30, 2020
Sales Surprise	-0.08%
EPS Surprise	2.83%
Quarterly EPS	1.09
Annual EPS (TTM)	5.51

Revenues

Total revenues in the quarter came in at \$4,789 million, lagging the Zacks Consensus Estimate of \$4,793 million by 0.1%. Quarterly revenues also decreased 9.7% from the year-ago quarter.

At the start of the year, organic sales were expected to be down 3%. The COVID-19 pandemic reduced its sales by an additional 4% in the first quarter. This 7% total fall in organic sales resulted in the year-over-year revenue decline.

Segment Details

Electrical Americas' total first-quarter sales were \$1,788 million, down 8.8% from the year-ago level. The decline was due to the impact of the divestiture of the Lighting business, negative currency translation and reduced organic sales.

Electrical Global's total sales were \$1,144 million, down 7.9% from the year-ago quarter. Organic sales were down 6% from the year-ago quarter, primarily due to the COVID-19 outbreak. Negative currency translation impacted sales by 3%, while the acquisition of Ulusoy added 1% to sales.

Hydraulics' total sales were \$507 million, down 16.2% from the year-ago quarter. The revenue decline was due to 14% fall in organic sales and a 2% impact from negative currency translation.

Aerospace total sales were \$680 million, up 12.6% from the year-ago quarter. The acquisition of Souriau-Sunbank contributed 14% to revenues but organic sales was down 1% from a year ago.

Vehicle total sales were \$598 million, down 26.2% from the year-ago quarter. Decline in organic sales, divestiture of the automotive fluid conveyance business and negative currency translation affected the results.

eMobility segment's total sales were \$72 million, down 13.2% from the year-ago quarter. The drop in the top line was due to decline in organic sales and negative currency translation.

Highlights of the Release

Eaton continues to make changes in its portfolio. The company sold the Lighting business for \$1.4 billion and entered into an agreement to sell the Hydraulics Business for \$3.3 billion by 2020-end.

Selling and administrative expenses were \$865 million, down 5.7% from the year-ago quarter. The company's research and development expenses in the first quarter were \$153 million, down 1.1% from the prior-year period. Interest expenses in the quarter were \$34 million, down 43.3% from the year-ago period.

Orders in Electrical Americas were up 3% year over year, while the same in Electrical Global, Hydraulics and Aerospace were down 1%, 11% and 1%, respectively.

Financial Update

In the first quarter, it repurchased shares worth \$1.3 billion, which equates to 3.4% shares outstanding of Eaton at the beginning of 2020.

Eaton's cash was \$239 million as of Mar 31, 2020 compared with \$370 million on Dec 31, 2019.

As of Mar 31, 2020, long-term debt of the company was \$7,842 million, up from \$7,819 million on Dec 31, 2019.

Guidance

Amid the novel coronavirus-led economic crisis and destruction of demand, the company has decided to withdraw its 2020 earnings guidance. Eaton expects free cash flow in the range of \$2.3-\$2.7 billion in 2020.

Valuation

Eaton Corporation shares are down 6.8% in the year to date period and up 7.2% over the trailing 12-month period. Stocks in the Zacks sub-industry was down 9.6% and the Zacks Industrial Products sector was down 11.7% in the year to date period. Over the past year, the Zacks sub-industry is up 3.1% and the sector is down 5.2%.

The S&P 500 index is down 2.7% in the year to date period and up 5.2% in the past year.

The stock is currently trading at 20.97X forward 12-month earnings, which compares to 23.23X for the Zacks sub-industry, 21.28X for the Zacks sector and 22.16X for the S&P 500 index.

Over the past five years, the stock has traded as high as 22.78X and as low as 9.92X, with a 5-year median of 14.4X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$93 price target reflects 22.14X forward 12-month earnings.

The table below shows summary valuation data for ETN

Valuation Multiples - ETN					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	20.97	23.23	21.28	22.16
	5-Year High	22.78	23.23	21.28	22.16
	5-Year Low	9.92	13.13	12.55	15.25
	5-Year Median	14.4	17.31	16.74	17.52
P/S F12M	Current	2.04	2.81	2.75	3.49
	5-Year High	2.23	2.81	2.75	3.49
	5-Year Low	1.08	1.46	1.52	2.53
	5-Year Median	1.54	2.02	2	3.02
P/B TTM	Current	2.47	5.4	5.53	4.29
	5-Year High	2.69	5.61	5.92	4.56
	5-Year Low	1.44	3.01	3.33	2.83
	5-Year Median	2.05	4.47	4.49	3.69

As of 7/2/2020

Industry Analysis Zacks Industry Rank: Top 33% (83 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
ABB Ltd (ABB)	Neutral	4
A. O. Smith Corporation (AOS)	Neutral	3
Dover Corporation (DOV)	Neutral	3
Emerson Electric Co. (EMR)	Neutral	4
Energys (ENS)	Neutral	3
SPX FLOW, Inc. (FLOW)	Neutral	3
Regal Beloit Corporation (RBC)	Neutral	3
Rexnord Corporation (RXN)	Neutral	3

Industry Comparison Industry: Manufacturing - Electronics				Industry Peers		
	ETN	X Industry	S&P 500	ABB	DOV	EMR
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	4	3	4
VGM Score	B	-	-	F	C	A
Market Cap	35.30 B	2.35 B	21.98 B	50.80 B	14.02 B	36.83 B
# of Analysts	9	3.5	14	3	7	7
Dividend Yield	3.31%	0.39%	1.91%	2.20%	2.01%	3.24%
Value Score	B	-	-	D	C	B
Cash/Price	0.01	0.11	0.07	0.14	0.04	0.07
EV/EBITDA	11.60	10.51	12.74	17.04	13.28	9.91
PEG Ratio	2.77	3.19	2.89	5.42	1.81	3.19
Price/Book (P/B)	2.47	2.45	2.98	4.22	4.70	4.87
Price/Cash Flow (P/CF)	11.16	13.07	11.75	13.90	12.36	12.17
P/E (F1)	24.24	24.27	21.41	33.63	20.83	20.05
Price/Sales (P/S)	1.69	1.76	2.30	1.86	1.98	2.05
Earnings Yield	4.13%	3.92%	4.42%	2.99%	4.80%	4.98%
Debt/Equity	0.57	0.19	0.76	0.62	0.99	0.52
Cash Flow (\$/share)	7.91	2.20	6.94	1.69	7.88	5.07
Growth Score	C	-	-	D	C	A
Hist. EPS Growth (3-5 yrs)	7.34%	6.15%	10.93%	3.42%	14.55%	2.96%
Proj. EPS Growth (F1/F0)	-35.88%	-21.16%	-9.56%	-43.82%	-21.13%	-16.69%
Curr. Cash Flow Growth	0.36%	2.39%	5.51%	-3.96%	10.20%	7.06%
Hist. Cash Flow Growth (3-5 yrs)	2.58%	2.76%	8.62%	-2.99%	1.28%	-0.68%
Current Ratio	1.75	2.12	1.30	1.18	1.29	1.01
Debt/Capital	36.40%	16.14%	44.46%	38.38%	49.85%	34.37%
Net Margin	10.19%	5.53%	10.62%	4.68%	10.59%	12.04%
Return on Equity	14.67%	9.49%	15.75%	19.64%	29.80%	26.66%
Sales/Assets	0.65	0.70	0.55	0.59	0.81	0.85
Proj. Sales Growth (F1/F0)	-21.73%	-3.02%	-2.54%	-14.36%	-10.52%	-10.56%
Momentum Score	B	-	-	C	C	A
Daily Price Chg	1.31%	0.73%	0.47%	0.73%	1.90%	0.72%
1 Week Price Chg	-4.30%	-1.61%	-3.90%	1.83%	-2.38%	-3.40%
4 Week Price Chg	-4.08%	0.06%	-3.77%	9.23%	-5.89%	-2.34%
12 Week Price Chg	8.35%	16.47%	8.02%	29.45%	8.96%	19.06%
52 Week Price Chg	7.19%	-3.50%	-7.59%	17.09%	-5.77%	-6.86%
20 Day Average Volume	2,489,501	232,697	2,649,865	2,533,080	947,996	3,369,715
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.12%	0.00%	0.00%	9.71%	0.00%	0.00%
(F1) EPS Est 12 week change	-25.32%	-14.39%	-9.53%	-9.91%	-15.33%	-7.26%
(Q1) EPS Est Mthly Chg	1.13%	0.00%	0.00%	NA	0.00%	0.00%

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	C
Momentum Score	B
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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