

Eaton Corporation plc (ETN)

\$99.76 (As of 08/10/20)

Price Target (6-12 Months): **\$105.00**

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:A

Value: B

Growth: B

Momentum: A

Summary

Eaton's second-quarter earnings and revenues were better than expected. Its wide market reach, R&D investments to develop technically advanced products and the spin-off of less profitable businesses will boost operations. The company has taken measures to combat the economic crisis and decline in demand caused by the pandemic. Eaton's restructuring actions are in sync with long-term growth objectives. Strong cash flow generation is supporting Eaton's shareholder-friendly moves. Its shares 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 it to forecast decremental margins for 2020.

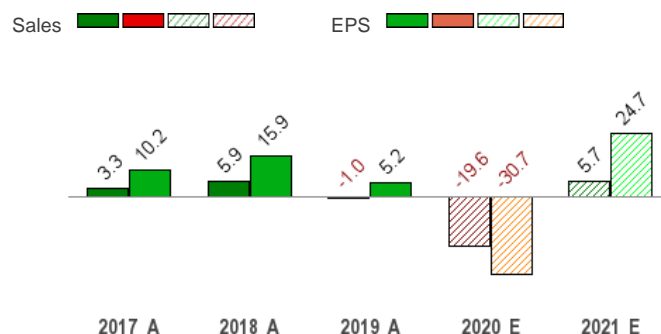
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$105.78 - \$56.42
20 Day Average Volume (sh)	1,443,587
Market Cap	\$39.9 B
YTD Price Change	5.3%
Beta	1.15
Dividend / Div Yld	\$2.92 / 2.9%
Industry	Manufacturing - Electronics
Zacks Industry Rank	Top 19% (49 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	34.6%
Last Sales Surprise	5.6%
EPS F1 Est- 4 week change	8.2%
Expected Report Date	11/03/2020
Earnings ESP	0.0%
P/E TTM	21.3
P/E F1	25.4
PEG F1	2.3
P/S TTM	2.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,402 E	4,439 E	4,642 E	4,820 E	18,184 E
2020	4,789 A	3,856 A	4,176 E	4,356 E	17,200 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	\$1.02 E	\$1.13 E	\$1.39 E	\$1.47 E	\$4.90 E
2020	\$1.09 A	\$0.70 A	\$1.04 E	\$1.09 E	\$3.93 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 08/10/2020. The reports text is as of 08/11/2020.

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.

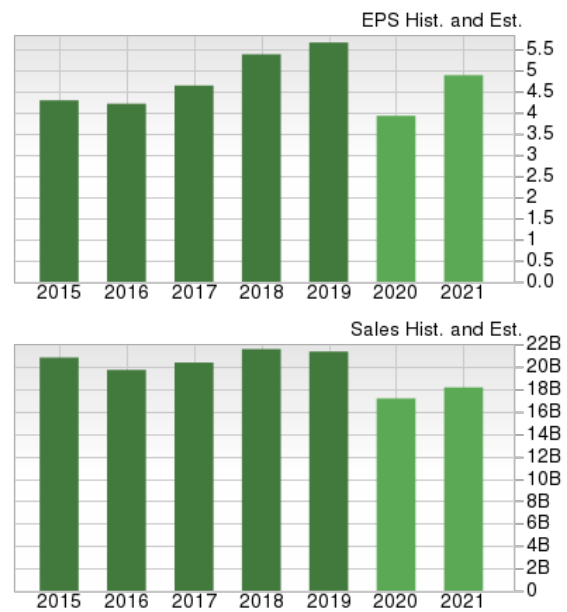
During first-quarter 2020, Eaton re-segmented certain reportable segments due to a reorganization of businesses. The new reportable segments are Electrical Americas and Electrical Global, which include Legacy Electrical Products and Electrical Systems and Services segments. The Filtration and Golf Grip 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. For first-half 2020, R&D expenses were \$279 million compared with \$307 million in the comparable year-ago period. Eaton has laid out a 10-year plan that includes \$3 billion investment in R&D programs, which will allow the company to create sustainable products over this period of time. The products supplied by Eaton have been deemed to be critical part of the global infrastructure and are absolutely essential in the crisis situation.

Eaton's wide market reach, restructuring actions, strong cash flow generation, share buybacks, R&D Programs and product innovation are likely to drive its performance.

Eaton's strategy to manufacture in the zone of sale has helped it to offset the impact of tariff on material prices. The company 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 28% compared with the industry's 25.2% rally.

- ▲ 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 has decided to implement a multi-year restructuring program to deal with the anticipated prolonged weakness in some of the end markets served. The cost of the program is estimated to be \$280 million, including the \$187 million charge it took in the second quarter. These actions will reduce structural cost and are targeted in those end markets, including Eaton's commercial aerospace, oil and gas, NAFTA Class 8 truck, as well as North America and European light vehicle markets, wherein recovery from the pandemic-induced weakness could take several years. The company expects the restructuring program to deliver mature-year benefits of \$200 million, when fully implemented in 2023.
- ▲ 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 is targeting share repurchases in the range of \$1.7-\$1.9 billion 2020, which includes \$1.3 billion already repurchased in first-quarter 2020. Eaton reaffirmed its capital spending view of \$400 million for 2020.

- ▲ At second quarter-end, Eaton's total debt to capital was 37.2%, up from 34.2% at the end of fourth-quarter 2019, as the company repurchased shares worth \$1.3 billion in first-half 2020. It exited the second quarter with a long-term debt of \$7,226 million, down from \$8,150 million at 2019-end. Eaton is trying to lower debts from the balance sheet. At second quarter-end, the company's cash and short-term investments were \$496 million, and it had enough liquidity to meet near-term obligation.

The times interest earned ratio of Eaton at second quarter-end was 10.7, down from 12 at the end of fourth-quarter 2019. The strong times interest earned ratio, although it declined from the 2019-end level, 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 prevailing economic uncertainty across the globe as a result of the COVID-19 pandemic, the company reaffirmed decremental margin expectation of 25-30% for the full year..

- ▼ 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 Q2 Earnings and Revenues Surpass Estimates

Eaton Corporation reported second-quarter 2020 earnings of 70 cents per share, which surpassed the Zacks Consensus Estimate of 52 cents by 34.6%. However, earnings were down 54.2% year over year due to weakness in some of its end markets. GAAP earnings in the reported quarter were 13 cents per share compared with \$1.50 in the year-ago period. The difference between GAAP and operating earnings in the reported quarter was due to a one-time charge of 20 cents associated with acquisitions and divestitures, as well as 37 cents related to a multi-year restructuring program.

Quarter Ending **06/2020**

Report Date	Jul 29, 2020
Sales Surprise	5.55%
EPS Surprise	34.62%
Quarterly EPS	0.70
Annual EPS (TTM)	4.68

Revenues

Total quarterly revenues came in at \$3,856 million, which beat the Zacks Consensus Estimate of \$3,653 million by 5.6%. However, total revenues decreased 30.3% from the year-ago quarter. In the reported quarter, organic sales were down 22% from the prior-year period. Divestiture of the Lighting and Automotive Fluid Conveyance businesses resulted in an 8% decline in revenues, and negative currency translation impacted the same by 2%. Acquired assets added 2% to second-quarter sales.

Segment Details

Electrical Americas' total second-quarter sales were \$1,490 million, down 28.5% from the year-ago level. The decline was due to the impact of the Lighting business divestiture, negative currency translation and reduced organic sales.

Electrical Global's total sales were \$1,111 million, down 16.1% from the year-ago quarter. Organic sales were down 14% from the year-ago quarter, primarily due to the COVID-19 outbreak. Negative currency translation impacted sales by 2%.

Hydraulics' total sales were \$411 million, down 31.8% from the year-ago quarter. The revenue decline was due to 30% fall in organic sales and a 2% impact from negative currency translation.

Aerospace total sales were \$461 million, down 27.3% from the year-ago quarter. The acquisition of Souriau-Sunbank contributed 8% to revenues. However, organic sales were down 27% from a year ago.

Vehicle total sales were \$327 million, down 59.3% 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 \$56 million, down 33% from the year-ago quarter. The deterioration in the top line was due to a decline in organic sales.

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 \$691 million, down 23.8% from the year-ago quarter. The company's second-quarter research and development expenses were \$126 million, down 16.6% from the prior-year period. Interest expenses for the quarter were \$38 million, down 24% from the year-ago period.

Orders in Electrical Americas were up 2.1% year over year, while the same in Electrical Global, Hydraulics and Aerospace was down 4.6%, 33.7% and 12.8%, respectively. Despite the novel coronavirus-related challenges early in the quarter, orders registered an impressive growth in June, with the residential and utility end markets witnessing the maximum improvement.

The company decided to implement a multi-year restructuring program that will cost nearly \$280 million. Total second-quarter expenses of \$187 million were incurred by Eaton.

Financial Update

Eaton's cash was \$292 million as of Jun 30, 2020 compared with \$370 million on Dec 31, 2019. As of Jun 30, 2020, long-term debt of the company was \$6,906 million, down from \$7,819 million on Dec 31, 2019.

Guidance

Amid the novel coronavirus-led economic crisis and destruction of demand, the company decided to withdraw its 2020 earnings guidance. Eaton expects free cash flow in the range of \$2.3-\$2.7 billion for 2020. It is targeting share buyback in the range of \$1.7-\$1.9 billion in 2020, of which \$1.3 billion is already completed in first-quarter 2020.

Valuation

Eaton Corporation shares are up 5.3% in the year to date period and up 28% over the trailing 12-month period. Stocks in the Zacks sub-industry was up 0.9% and the Zacks Industrial Products sector was down 1.6% in the year to date period. Over the past year, the Zacks sub-industry is up 25.2% and the sector is up 14.4%.

The S&P 500 index is up 4.2% in the year to date period and up 16.7% in the past year.

The stock is currently trading at 22.07X forward 12-month earnings, which compares to 23.82X for the Zacks sub-industry, 22.18X for the Zacks sector and 22.81X for the S&P 500 index.

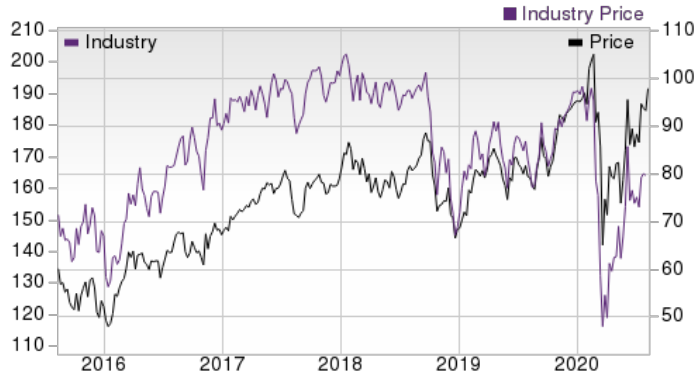
Over the past five years, the stock has traded as high as 22.78X and as low as 9.92X, with a 5-year median of 14.49X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$105 price target reflects 23.23X forward 12-month earnings.

The table below shows summary valuation data for ETN

Valuation Multiples - ETN					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	22.07	23.82	22.18	22.81
	5-Year High	22.78	23.82	22.18	22.81
	5-Year Low	9.92	13.13	12.55	15.25
	5-Year Median	14.49	17.36	17.48	17.58
P/S F12M	Current	2.24	3	2.96	3.67
	5-Year High	2.24	3	2.96	3.67
	5-Year Low	1.08	1.46	1.52	2.53
	5-Year Median	1.55	2.04	2.04	3.05
P/B TTM	Current	2.8	6.06	5.44	4.68
	5-Year High	2.8	6.06	5.94	4.68
	5-Year Low	1.44	3.01	3.34	2.83
	5-Year Median	2.06	4.5	4.51	3.74

As of 8/10/2020

Industry Analysis Zacks Industry Rank: Top 19% (49 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Regal Beloit Corporation (RBC)	Outperform	2
Rexnord Corporation (RXN)	Outperform	1
ABB Ltd (ABB)	Neutral	2
A. O. Smith Corporation (AOS)	Neutral	3
Emerson Electric Co. (EMR)	Neutral	3
Energysys (ENS)	Neutral	3
Murata Manufacturing Inc. (MRAAY)	Neutral	3
Energous Corporation (WATT)	Neutral	2

Industry Comparison Industry: Manufacturing - Electronics				Industry Peers		
	ETN	X Industry	S&P 500	ABB	EMR	MRAAY
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	2	3	3
VGM Score	A	-	-	C	A	C
Market Cap	39.91 B	2.96 B	23.56 B	56.50 B	40.74 B	42.21 B
# of Analysts	9	3.5	14	3	8	1
Dividend Yield	2.93%	0.34%	1.71%	1.98%	2.93%	0.96%
Value Score	B	-	-	C	B	D
Cash/Price	0.01	0.08	0.07	0.08	0.06	0.08
EV/EBITDA	12.57	11.68	13.39	19.20	11.36	11.36
PEG Ratio	2.37	2.76	2.92	5.25	2.69	NA
Price/Book (P/B)	2.80	2.75	3.18	4.49	5.17	2.59
Price/Cash Flow (P/CF)	12.62	15.10	12.69	15.45	13.46	13.37
P/E (F1)	26.07	25.36	22.16	32.58	20.66	33.94
Price/Sales (P/S)	2.08	2.12	2.55	2.15	2.37	2.99
Earnings Yield	3.94%	3.63%	4.33%	3.07%	4.84%	2.95%
Debt/Equity	0.51	0.20	0.77	0.50	0.70	0.09
Cash Flow (\$/share)	7.91	2.20	6.94	1.69	5.07	1.17
Growth Score	B	-	-	D	B	A
Hist. EPS Growth (3-5 yrs)	7.09%	5.93%	10.41%	2.54%	4.48%	NA
Proj. EPS Growth (F1/F0)	-30.63%	-15.88%	-6.51%	-35.48%	-10.57%	-30.30%
Curr. Cash Flow Growth	0.36%	2.39%	5.26%	-3.96%	7.06%	12.53%
Hist. Cash Flow Growth (3-5 yrs)	2.58%	3.59%	8.55%	-2.99%	-0.68%	12.59%
Current Ratio	1.50	2.26	1.34	1.19	1.32	3.49
Debt/Capital	33.67%	16.52%	44.59%	33.15%	41.11%	8.22%
Net Margin	8.03%	5.70%	10.13%	5.83%	11.39%	11.92%
Return on Equity	12.73%	8.68%	14.59%	18.45%	26.12%	11.19%
Sales/Assets	0.61	0.67	0.51	0.57	0.81	0.71
Proj. Sales Growth (F1/F0)	-19.59%	-6.55%	-1.54%	-10.91%	-9.16%	-6.55%
Momentum Score	A	-	-	C	A	D
Daily Price Chg	2.05%	0.27%	0.91%	0.27%	2.71%	0.21%
1 Week Price Chg	4.97%	5.72%	2.30%	4.00%	7.03%	-5.75%
4 Week Price Chg	14.10%	13.81%	8.54%	7.78%	12.07%	3.40%
12 Week Price Chg	27.46%	23.11%	13.68%	39.51%	20.83%	10.61%
52 Week Price Chg	27.98%	24.95%	3.71%	40.90%	16.91%	48.27%
20 Day Average Volume	1,443,587	202,034	2,015,804	1,909,923	2,570,279	191,753
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	7.73%	0.00%
(F1) EPS Est 4 week change	8.19%	4.52%	1.67%	12.15%	7.92%	0.00%
(F1) EPS Est 12 week change	1.95%	3.37%	2.27%	25.98%	8.13%	NA
(Q1) EPS Est Mthly Chg	16.08%	0.96%	0.67%	NA	3.87%	NA

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	B
Momentum Score	A
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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