

Eaton Corporation plc (ETN)

\$97.90 (As of 01/23/20)

Price Target (6-12 Months): **\$104.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/23/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: B

Growth: B

Momentum: F

Summary

Eaton's ongoing R&D investments will help it to upgrade its products and provide better electrical solutions to customers. Eaton's divestment of the Lighting and Hydraulics business to focus on core operations is in sync with long-term growth objectives. Wide market reach, strategic acquisitions, strong cash flow generation, share buybacks and prudent product innovation are likely to drive its performance. Notably, shares of Eaton have outperformed its industry in the last six months. However, Eaton's world-wide operations expose it to negative currency translation, cyber-attacks and security breaches, all of which might impact its operation. Weak end-market conditions have compelled the company to lower organic growth projection and trim earnings expectation.

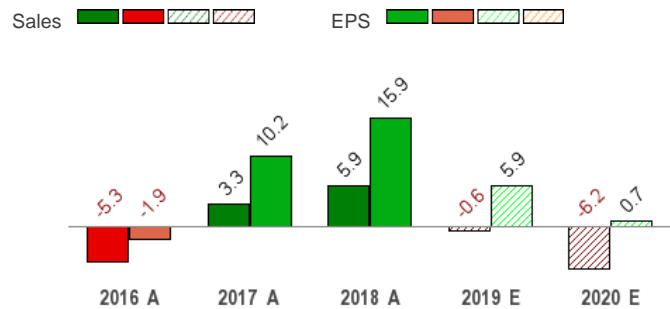
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$99.82 - \$67.97
20 Day Average Volume (sh)	2,244,782
Market Cap	\$40.5 B
YTD Price Change	3.4%
Beta	1.43
Dividend / Div Yld	\$2.84 / 2.9%
Industry	Manufacturing - Electronics
Zacks Industry Rank	Bottom 25% (192 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	0.7%
Last Sales Surprise	-4.2%
EPS F1 Est- 4 week change	-1.4%
Expected Report Date	02/04/2020
Earnings ESP	-1.2%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	4,964 E	5,091 E	4,982 E	5,052 E	20,163 E
2019	5,305 A	5,533 A	5,314 A	5,328 E	21,488 E
2018	5,251 A	5,487 A	5,412 A	5,459 A	21,609 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$1.20 E	\$1.48 E	\$1.54 E	\$1.52 E	\$5.75 E
2019	\$1.26 A	\$1.53 A	\$1.52 A	\$1.40 E	\$5.71 E
2018	\$1.10 A	\$1.39 A	\$1.43 A	\$1.46 A	\$5.39 A

*Quarterly figures may not add up to annual.

P/E TTM	17.0
P/E F1	17.0
PEG F1	2.0
P/S TTM	1.9

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 01/23/2020. The reports text is as of 01/24/2020.

Overview

Dublin, Ireland-based Eaton Corporation plc is a diversified power management company and a global technology leader in electrical components and systems for power quality, distribution and control; hydraulics components, systems and services for industrial and mobile equipment; aerospace fuel, and hydraulic and pneumatic systems for commercial and military use. The company sells its products to customers in more than 175 countries and has approximately 99,000 employees in 59 countries. The company was founded in 1916.

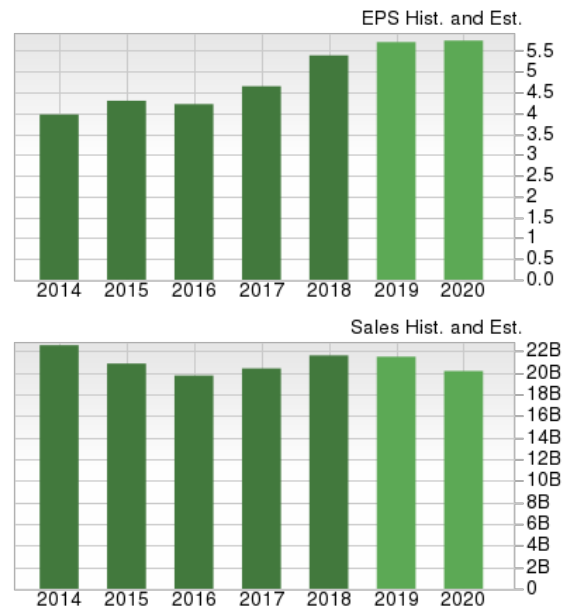
Eaton's reportable segments are **Electrical Products**, **Electrical Systems and Services**, **Hydraulics**, **Aerospace**, **Vehicle** and **eMobility**.

Electrical Products segment consists of electrical components, industrial controls, residential products, single phase power quality, emergency lighting, fire detection, wiring devices, structural support systems, circuit protection, and lighting products. **Electrical Systems and Services** segment consists of power distribution and assemblies, three phase power quality, hazardous duty electrical equipment, intrinsically safe explosion-proof instrumentation, utility power distribution, power reliability equipment and services.

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. **Hydraulics** segment manufactures and markets a comprehensive line of reliable, high-efficiency hydraulic systems and components. **Aerospace** segment is a supplier of aerospace fuel, hydraulics and pneumatic systems for commercial and military use.

The **eMobility** segment was launched in the first quarter of 2018. This segment will focus on two technologies within electrical vehicles, namely Power electronics & conversion and Power distribution & circuit protection.

Eaton's segments — Electrical Products, Electrical Systems and Services, Vehicle, Hydraulics, Aerospace and eMobility — had contributed 32.9%, 27.9%, 16.1%, 12.8%, 8.8% and 1.5%, respectively, to total 2018 revenues.



Reasons To Buy:

- ▲ In the last six months, Eaton's shares have gained 19.4% compared with its industry's rally of 17.9%. 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 also been upgrading the existing systems to maintain its strong position in the global markets. In 2018, the company's R&D expenses amounted to \$584 million, which was in line with the prior-year period. During the first nine months of 2019, the company invested \$454 million, up 3.4% from the comparable prior-year period.

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. Orders in Electrical Products (excluding Lighting), Electrical Systems and Services, and Aerospace were up 1%, 5% and 13% year over year, respectively, which reflected strong demand for high-quality products offered by the company.

- ▲ 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.

In addition to making accretive acquisitions like Turkey-based Ulusoy Elektrik Imalat Taahhut ve Ticaret A.S. and Souriau-Sunbank Connection Technologies from TransDigm Group, the company intends to sell off the less profitable lighting business. The company also announced that it has entered into a definite agreement to sell the Hydraulics business for \$3.3 billion in cash. These divestitures will allow Eaton to focus on higher-margin core businesses.

- ▲ Eaton continues to generate a stable cash inflow through its proficient handling of operating activities. In 2018, Eaton's operating cash flow was \$3 billion. It expects 2019 free cash flow in the range of \$2.85-\$3.05 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.

In 2018, the company had returned \$2.45 billion through share buybacks and dividends. Strong cash flow generating capacity will allow the company to continue with share-repurchase initiatives. Eaton aims to repurchase shares worth \$1 billion in 2019. During the first nine months of 2019, the company repurchased shares worth \$978 million and paid dividend of \$907 million to its shareholders.

- ▲ Eaton expects 2019 operating margins in the range of 17.3-17.7%, up from its previous range of 17.1-17.5%, courtesy of strong execution and pro-active cost controls. The higher margin expectation for 2019 is due to improved margins from its segments, except vehicles and hydraulics.

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

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. It expects organic revenue growth in excess of 1% in 2019, down from prior expectation of 3% due to decline in growth rates in all segments, thanks to weak end-market conditions.
- ▼ 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. Eaton expects a \$350-million negative impact from foreign exchange translation, which is likely to in turn affect earnings in 2019.

Widespread operation exposes it to geo-political risks, negative currency translation and shortage of raw materials, which might impact its ability to produce products at competitive prices.

Last Earnings Report

Eaton's Q3 Earnings Beat, Revenues Miss, View Cut

Eaton Corporation reported third-quarter 2019 earnings of \$1.52 per share, which surpassed the Zacks Consensus Estimate by a penny. The reported earnings were at the lower end of management's guided range of \$1.50-\$1.60 per share. Moreover, the bottom line marked a 6% improvement from the year-ago level.

GAAP earnings in the reported quarter were \$1.44 per share compared with 96 cents in the year-ago period. The difference between GAAP and operating earnings in the reported quarter was due to one-time acquisition and divestiture transaction and integration costs.

Quarter Ending **09/2019**

Report Date	Oct 29, 2019
Sales Surprise	-4.16%
EPS Surprise	0.66%
Quarterly EPS	1.52
Annual EPS (TTM)	5.77

Revenues

Total revenues in the quarter came in at \$5,314 million, lagging the Zacks Consensus Estimate of \$5,545 million by 4.2%. Quarterly revenues also decreased 1.8% from the year-ago quarter. The year-over-year decline in revenues was due to 1% fall in organic sales and negative currency translation of 1.5%. These negatives were partially offset by gains from acquired assets.

Segment Details

Electrical Products' total third-quarter sales were \$1,786 million, down 0.2% from the year-ago level. Although organic sales were up 1% from the prior-year quarter, the metric was negatively impacted by 1% due to currency translation.

Electrical Systems and Services' total sales were \$1,572 million, up 3.5% from the year-ago quarter. Organic sales were also up 3% from the year-ago quarter. The acquisition of Ulusoy and Innovative Switchgear added 1.5% to its sales, which were negatively impacted by 1.5% due to currency translation.

Hydraulics total sales were \$603 million, down 10% from the year-ago quarter. Organic sales were down 8% year over year and negative currency translation adversely impacted revenues by another 2%.

Aerospace total sales were \$513 million, up 7.3% from the year-ago quarter due to 8% organic sales growth, marginally offset by negative currency translation of 1%.

Vehicle total sales were \$761 million, down 13.1% from the year-ago quarter, owing to a 12% decline in organic sales and 1% negative currency translation.

eMobility segment's total sales were \$79 million, down 1.2% from the year-ago quarter. Organic sales were flat with the prior-year level. Revenues were negatively impacted by 1% due to currency translation.

Quarterly Highlights

Segment margins in the reported quarter were 18.7%, up 110 basis points (bps) from the year-ago level. Cost of products sold in the reported quarter was \$3,512 million, down 2.4% from the year-ago figure.

Selling and administrative expenses were \$885 million, down 0.5% from the year-ago quarter. The company's research and development expenses in the first nine months of the year were \$454 million, up 3.4% from the corresponding period of 2019. Interest expenses in the first nine months of 2019 were \$183 million, down 10.7% from the comparable prior-year period.

Orders in Electrical Products (excluding Lighting), Electrical Systems and Services, and Aerospace were up 1%, 5% and 13% year over year, respectively. On the contrary, Hydraulics' orders were down 14% year over year due to weakness in the global mobile equipment market.

It repurchased shares worth \$539 million in the quarter, resulting in a repurchase of \$978 million shares year to date.

Financial Update

Eaton's cash & cash equivalents were \$549 million as of Sep 30, 2019 compared with \$283 million on Dec 31, 2018. As of Sep 30, 2019, long-term debt of the company was \$8,013 million, up from \$6,768 million on Dec 31, 2018.

Guidance

Fourth-quarter 2019 earnings per share are expected between \$1.36 and \$1.46. The company now expects 2019 earnings within \$5.67-\$5.77, down from the prior guided range of \$5.77-\$5.97 per share. Segment operating margin for 2019 is expected within 17.3-17.7%.

Eaton has plans to repurchase shares worth \$1 billion in 2019. Currency translation is likely to have a negative impact of \$350 million in 2019.

The company expects organic revenues to improve 1% in 2019, down 200 bps from the prior expectation.

Recent News

Eaton to Sell Hydraulics for \$3.3B, Focus on Core Business - Jan 22, 2020

Eaton Corporation Plc announced that it has entered into a definite agreement to sell the Hydraulics business for \$3.3 billion in cash to Danfoss A/S, a Danish industrial company. This deal is part of Eaton's ongoing transformation that will propel the company to boost growth and lead to earnings consistency.

The deal is expected to close by the end of this year, and is subject to customary closing conditions and regulatory approvals. Earlier this year, Eaton announced that it has completed the sale of the Automotive Fluid Conveyance Division to Quantum Capital Partners.

Valuation

Eaton Corporation shares are up 19.4% in the last six months period and 37.7% over the trailing 12-month period. Stocks in the Zacks sub-industry was up 17.9% and the Zacks Industrial Products sector was up 8.8% in the last six months period. Over the past year, the Zacks sub-industry and sector are up 21.2% and 15.2%, respectively.

The S&P 500 index is up nearly 11.5% in the last six months period and up 23.9% in the past year.

The stock is currently trading at 16.92X forward 12-month earnings, which compares to 20.27X for the Zacks sub-industry, 18.1X for the Zacks sector and 19.13X for the S&P 500 index.

Over the past five years, the stock has traded as high as 17.82X and as low as 10.39X, with a 5-year median of 14.23X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$104 price target reflects 17.96X 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	16.92	20.27	18.1	19.13
	5-Year High	17.82	20.3	19.91	19.34
	5-Year Low	10.39	13.14	12	15.17
	5-Year Median	14.23	17.03	16.54	17.44
P/S F12M	Current	2	2.63	2.76	3.56
	5-Year High	2	2.63	2.76	3.56
	5-Year Low	1.08	1.45	1.51	2.54
	5-Year Median	1.52	1.96	1.97	3
P/B TTM	Current	2.55	5.21	5.67	4.54
	5-Year High	2.55	5.23	5.74	4.55
	5-Year Low	1.44	3.18	3.44	2.85
	5-Year Median	2.04	4.38	4.45	3.61

As of 1/23/2020

Industry Analysis Zacks Industry Rank: Bottom 25% (192 out of 255)



Top Peers

SPX FLOW, Inc. (FLOW)	Outperform
ABB Ltd (ABB)	Neutral
A. O. Smith Corporation (AOS)	Neutral
Dover Corporation (DOV)	Neutral
Emerson Electric Co. (EMR)	Neutral
Energysys (ENS)	Neutral
Regal Beloit Corporation (RBC)	Neutral
Rexnord Corporation (RXN)	Neutral

Industry Comparison Industry: Manufacturing - Electronics				Industry Peers		
	ETN Neutral	X Industry	S&P 500	ABB Neutral	DOV Neutral	EMR Neutral
VGM Score	B	-	-	D	B	A
Market Cap	40.47 B	2.25 B	24.46 B	50.95 B	17.24 B	47.26 B
# of Analysts	10	4	13	1	8	10
Dividend Yield	2.90%	0.00%	1.75%	2.06%	1.65%	2.58%
Value Score	B	-	-	C	C	B
Cash/Price	0.02	0.08	0.04	0.06	0.02	0.03
EV/EBITDA	13.34	11.54	14.11	17.08	17.39	12.98
PEG Ratio	1.95	1.87	2.04	3.71	1.64	2.69
Price/Book (P/B)	2.55	2.32	3.40	3.72	5.71	5.77
Price/Cash Flow (P/CF)	13.03	13.00	13.66	13.58	16.72	15.32
P/E (F1)	17.03	18.66	19.10	23.02	18.84	21.36
Price/Sales (P/S)	1.87	1.87	2.67	1.80	2.40	2.57
Earnings Yield	5.87%	4.69%	5.23%	4.32%	5.31%	4.68%
Debt/Equity	0.52	0.27	0.72	0.62	0.96	0.52
Cash Flow (\$/share)	7.52	1.83	6.94	1.76	7.10	5.07
Growth Score	B	-	-	D	B	A
Hist. EPS Growth (3-5 yrs)	5.47%	5.47%	10.60%	3.70%	8.45%	-1.19%
Proj. EPS Growth (F1/F0)	0.65%	7.70%	7.59%	13.74%	7.58%	-1.57%
Curr. Cash Flow Growth	8.89%	12.53%	13.90%	7.17%	12.99%	7.06%
Hist. Cash Flow Growth (3-5 yrs)	1.88%	3.18%	9.00%	-1.95%	-2.75%	-0.68%
Current Ratio	1.72	2.16	1.22	1.36	1.42	1.19
Debt/Capital	34.42%	24.28%	42.99%	38.35%	49.08%	34.08%
Net Margin	11.06%	6.86%	11.35%	5.06%	9.08%	12.55%
Return on Equity	15.15%	10.17%	17.10%	19.16%	29.62%	26.32%
Sales/Assets	0.68	0.88	0.55	0.63	0.83	0.88
Proj. Sales Growth (F1/F0)	-6.17%	0.64%	4.03%	-0.65%	2.55%	0.66%
Momentum Score	F	-	-	D	B	C
Daily Price Chg	0.76%	-0.14%	0.26%	-0.17%	0.66%	0.74%
1 Week Price Chg	0.74%	1.61%	2.29%	-0.25%	3.25%	1.09%
4 Week Price Chg	3.01%	0.27%	2.24%	-0.96%	2.46%	1.20%
12 Week Price Chg	12.39%	13.64%	7.79%	13.53%	14.21%	10.61%
52 Week Price Chg	39.54%	22.41%	21.61%	25.75%	49.85%	23.08%
20 Day Average Volume	2,244,782	162,684	1,536,379	1,338,103	584,707	2,242,543
(F1) EPS Est 1 week change	-0.09%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-1.37%	0.00%	0.00%	0.98%	0.04%	0.19%
(F1) EPS Est 12 week change	-5.38%	-2.94%	-0.23%	-0.16%	-0.32%	-3.76%
(Q1) EPS Est Mthly Chg	-0.42%	0.00%	0.00%	NA	0.00%	0.60%

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	F
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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