

Flowserve Corporation (FLS)

\$23.93 (As of 04/21/20)

Price Target (6-12 Months): **\$21.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 04/19/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM: C

Value: C

Growth: B

Momentum: C

Summary

Over the past three months, Flowserve's shares have underperformed the industry. Some of the company's manufacturing facilities, global technology and engineering centers, quick response centers, and corporate headquarters have suffered temporary shutdowns on account of the coronavirus outbreak. Also, it has withdrawn its guidance for 2020 on end-market uncertainties stemming from the outbreak. Moreover, Flowserve's realignment plan is fuelling expenses and adversely impacting profitability in the near term. Given the company's extensive geographic presence, its business is subject to political, economic and geopolitical issues. In addition, rise in debt levels can increase its financial obligations. In the past 30 days, earnings estimates for the company have been lowered for 2020 and 2021.

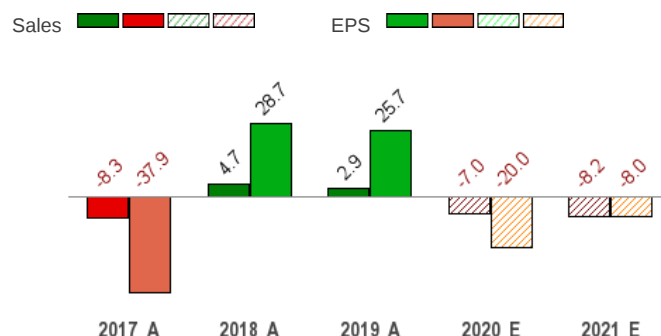
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$54.16 - \$18.98
20 Day Average Volume (sh)	1,855,436
Market Cap	\$3.2 B
YTD Price Change	-50.1%
Beta	1.90
Dividend / Div Yld	\$0.80 / 3.2%
Industry	Manufacturing - General Industrial
Zacks Industry Rank	Bottom 22% (197 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	1.5%
Last Sales Surprise	1.9%
EPS F1 Est- 4 week change	-23.0%
Expected Report Date	05/07/2020
Earnings ESP	-9.8%
P/E TTM	11.3
P/E F1	13.6
PEG F1	0.9
P/S TTM	0.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					3,366 E
2020	897 E	872 E	894 E	985 E	3,667 E
2019	890 A	990 A	997 A	1,068 A	3,945 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.32 E	\$0.22 E	\$0.39 E	\$0.56 E	\$1.62 E
2020	\$0.41 E	\$0.37 E	\$0.49 E	\$0.60 E	\$1.76 E
2019	\$0.41 A	\$0.54 A	\$0.59 A	\$0.66 A	\$2.20 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 04/21/2020. The reports text is as of 04/22/2020.

Overview

Founded in 1912 and headquartered at Irving, TX, Flowserve Corporation is a leading manufacturer and aftermarket service provider of comprehensive flow control systems, globally.

The company develops and manufactures precision-engineered flow control equipment, such as pumps, valves and seals, for critical service applications that require high reliability. Flowserve uses its manufacturing platform to offer a broad array of aftermarket equipment services, such as installation, advanced diagnostics, repair and retrofitting.

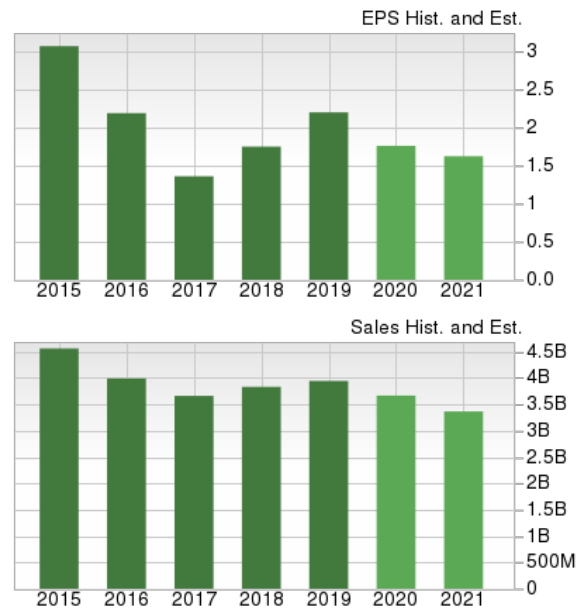
The company uses a footprint of Quick Response Centers (QRCs) around the globe to deliver these aftermarket services. The company sells products and services to more than 10,000 companies across more than 50 countries in North America, Europe, the Middle East, Africa, the Asia Pacific and Latin America.

During the first quarter of 2019, the company combined operations of Engineered Product Division and Industrial Product Division under one segment — Flowserve Pump Division (FPD). The changes will enable the company to better control operations and serve customers.

Flowserve currently has two reportable segments:

Flowserve Pump Division: This segment is engaged in the manufacturing of highly engineered pumps, pump systems, industrial pumps, mechanical seals and auxiliary systems. Also, the segment provides parts of replacement purposes and related services. The segment has 39 manufacturing facilities and 144 QRCs. End markets served include power generation, chemical, general, and oil & gas markets.

Flow Control Division: The segment is engaged in the manufacturing of valve, valve automation products, boiler controls and solutions. Notably, this segment has 49 manufacturing facilities and QRCs in 22 countries throughout the world. Several end markets served by the segment include power generation, water management, chemical as well as oil and gas.



Reasons To Sell:

- ▼ In the past three months, Flowserve's shares have moved down 49.9% compared with the industry's decline of 22.3%. Several of the company's manufacturing facilities, global technology and engineering centers, quick response centers, and corporate headquarters have suffered temporary shutdowns, owing to the coronavirus outbreak. Earlier, the company had anticipated adjusted earnings of \$2.30-\$2.45 per share for 2020, reflecting year-over-year growth of 8% at mid-point. Also, for the year, the company had expected revenue growth of 3-5%. However, it has withdrawn its guidance for 2020 on end-market uncertainties, owing to the outbreak. Notably, the duration of the coronavirus pandemic and the impacts on the demand for the company's products and services will likely have a bearing on its results.
- ▼ Flowserve's realignment plan is likely to provide benefits in the long run. However, the plan is fuelling expenses and adversely impacting profitability in the near term. In fourth-quarter 2019, the company's net income was adversely impacted by realignment expenses of \$3.1 million or 2 cents per share. In addition, it currently suffers from adverse impacts of unfavorable movements in foreign currencies. In the fourth quarter, the company's sales were adversely impacted by 1.1% from forex woes.
- ▼ A highly leveraged balance sheet can be detrimental to Flowserve's profitability. At the end of fourth-quarter 2019, the company's long-term debts were at \$1,366 million, reflecting sequential increase of 1.2%. Net interest and other expenses increased 4.2% year over year to \$12.8 million in the quarter. Fresh issuance in the quarters ahead is bound to increase this balance and inflate the company's financial obligations.
- ▼ Flowserve's business depends on capital investment and maintenance expenditure by customers. These investment decisions are impacted by numerous factors, including the state of domestic and global economies, global energy demand, the cyclical nature of the markets, liquidity and condition of global credit, and capital markets. In addition, macroeconomic and political issues may pose as threats for the company. In addition, analysts have become increasingly bearish about Flowserve. In the past 30 days, the company's earnings estimates have been decreased by 24.1% for 2020 and 37.2% for 2021.

Realignment costs as well as headwinds related to coronavirus outbreak in China and high debt levels can be detrimental to Flowserve in the quarters ahead.

Risks

- In fourth-quarter 2019, Flowserve's earnings surpassed the Zacks Consensus Estimate by 1.5% and increased 13.8% year over year. The bottom-line results were driven by progress on the Flowserve 2.0 transformation strategy and improved operating leverage. The company will likely benefit from its solid backlog and the Flowserve 2.0 transformation program in the quarters ahead. For instance, it continues to expect a strong backlog of \$2.2 billion for the first quarter of 2020, suggesting a rise from \$2.16 billion recorded in the fourth quarter of 2019. Also, the company follows a disciplined capital-allocation strategy. Funds are primarily invested in enhancing organic growth and Flowserve 2.0, a multi-year program. It is worth mentioning here that Flowserve 2.0 is expected to enhance the company's ability to effectively support customers and create a better workplace for employees as well as drive significant long-term value for shareholders. Also, Flowserve is committed toward rewarding shareholders handsomely. In 2019, it paid out dividends of \$99.6 million and repurchased shares worth \$15 million. Further, capital expenditure in the period amounted to \$66.2 million. In addition, exiting 2019, it is left to buy back shares worth \$145.7 million from the \$500-million program authorized in November 2014.
 - Flowserve's solid liquidity position enables it to cover its immediate liabilities. For instance, exiting the fourth quarter of 2019, the company had total available liquidity of \$1.3 billion. Notably, this consists of cash and cash equivalents of about \$671 million, and around \$710 million of available capacity under the company's revolving credit facility. For four years (between 2019 and 2022), Flowserve anticipates revenues to rise roughly 200 basis points above the industry's growth rate. Operating margin is predicted to be 15-17% in 2022. Further, after-tax return on invested capital is projected to be 15-20% in 2022 while free cash flow will likely be more than 100% of net income.
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Last Earnings Report

Flowserve Q4 Earnings & Sales Beat Estimates, Rise Y/Y

Flowserve reported better-than-expected results in the fourth quarter of 2019, with earnings beating estimates by 1.5%. This was the fourth consecutive quarter of impressive results.

The machinery company's adjusted earnings in the reported quarter were 66 cents per share, surpassing the Zacks Consensus Estimate of 65 cents. Further, the bottom line grew 13.8% from the year-ago figure of 58 cents, driven by progress on the Flowserve 2.0 transformation strategy and improved operating leverage.

For 2019, the company's adjusted earnings per share were \$2.20, beating the Zacks Consensus Estimate of \$2.19. Also, the bottom line improved 25.7% year over year.

Quarter Ending **12/2019**

Report Date	Feb 17, 2020
Sales Surprise	1.90%
EPS Surprise	1.54%
Quarterly EPS	0.66
Annual EPS (TTM)	2.20

Segmental Revenues

In the quarter under review, Flowserve's sales were \$1,068.2 million, reflecting year-over-year growth of 8.2%. Notably, unfavorable movements in foreign currencies adversely impacted sales by 1.1%.

The company's revenues surpassed the Zacks Consensus Estimate of \$1,048 million by 1.9%.

Aftermarket sales in the reported quarter rose 5.3% year over year (or grew 6.6% on a constant-currency basis) to \$522 million. Furthermore, original equipment sales totaled \$546 million, reflecting year-over-year growth of 11.3% (or 12.1% on a constant-currency basis).

Bookings totaled \$1.05 billion in the quarter, reflecting a marginal increase of 0.7% (or 1.7% on a constant-currency basis) from the year-ago quarter. Of the end markets, booking strengthened in oil & gas, chemical, and water end markets. Backlog at the end of the reported quarter was \$2.16 billion.

The company currently has two reportable segments — Flowserve Pump Division and Flow Control Division. A brief discussion on the segments is provided below:

Revenues from the **Flowserve Pump Division** were \$739.5 million, improving 11.6% year over year or 12.7% on a constant-currency basis. Bookings grew 3.8% year over year to \$756 million.

Revenues from the **Flow Control Division** were \$330.2 million, rising 1.3% year over year or 2.2% on a constant-currency basis. Bookings of \$298.6 million declined 6.1% year over year.

For 2019, the company's sales totaled \$3.94 billion, reflecting growth of 2.9% from the previous year. Also, the top line surpassed the Zacks Consensus Estimate of \$3.92 billion.

Margin Profile

In the quarter under review, Flowserve's adjusted cost of sales increased 9.2% year over year to \$714 million. It represented 66.8% of sales compared with 66.3% in the year-ago quarter. Adjusted gross profit grew 6.4% year over year to \$354.2 million, while margin fell 50 basis points (bps) year over year to 33.2%. Selling, general and administrative expenses rose 5.3% year over year to \$230.2 million. It represented 21.6% of sales.

Adjusted operating income in the quarter under review improved 7.5% year over year to \$126.5 million. Moreover, adjusted operating margin fell 10 bps to 11.8%. Net interest and other expenses in the quarter grew 4.2% year over year to \$12.8 million. Effective tax rate was 22.2% versus 26.1% in the year-ago quarter.

Balance Sheet and Cash Flow

Exiting the fourth quarter of 2019, Flowserve had cash and cash equivalents of \$671 million, up 22.6% from \$547.3 million at the end of the last reported quarter. Long-term debt grew 1.2% sequentially to \$1,366 million.

During 2019, the company repaid debts of \$105 million.

In 2019, it generated net cash of \$312.7 million from operating activities, up 63.9% from the previous year. Capital expenditure in the year totaled \$66.2 million, declining 21.2% from \$84 million spent in 2018.

During the year, the company used \$99.6 million for distributing dividends and \$15 million for repurchasing shares.

Outlook

Flowserve is progressing well with transformation initiatives. The multi-year Flowserve 2.0 strategy will likely help in simplifying the operating model and spur growth. This along with solid backlog will help drive performance in 2020. However, geopolitical and macroeconomic issues are concerning.

The company anticipates adjusted earnings per share of \$2.30-\$2.45 for 2020. Revenues are anticipated to increase 3-5%.

Net interest expenses in the year will likely be \$45-\$50 million, while adjusted tax rate for the year is expected to be 24-26%. Capital expenditure is predicted to be \$90-\$100 million.

Recent News

Dividend

On **Apr 9, 2020**, Flowserve paid a quarterly cash dividend of 20 cents per share to shareholders of record as on Mar 27. The company's previous quarterly dividend rate was 19 cents.

Guidance Withdrawn

On **Apr 6, 2020**, Flowserve announced the withdrawal of its earlier announced guidance for 2020 on end-market uncertainties due to the coronavirus pandemic.

The company noted that several of its manufacturing facilities, global technology and engineering centers, quick response centers, and corporate headquarters have suffered temporarily shutdowns, owing to the coronavirus outbreak. However, it remains committed to protect the safety, health and well-being of employees, customers and partners amid the crisis.

On the fourth-quarter 2019 conference call held in February, Flowserve had anticipated adjusted earnings of \$2.30-\$2.45 per share for 2020, suggesting year-over-year growth of 8% at the mid-point.

Also, for the year, the company had expected revenues growth of 3-5%, while net interest expenses were estimated to be \$45-\$50. Also, the company's capital expenditure was projected to be \$90-\$100 million.

However, on uncertainties, regarding the impacts of the outbreak on financial and operating results, Flowserve has now withdrawn its guidance for 2020.

Valuation

Flowserve shares are down 50.1% and 50.2% in the year-to-date period and over the trailing 12-month period, respectively. Stocks in the Zacks sub-industry and the Zacks Industrial Products sector are down 21.1% and 23.5% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector are down 15.8% and 22.1%, respectively.

The S&P 500 index has moved down 10.8% year to date and decreased 1.7% in the past year.

The stock is currently trading at 10.04x forward 12-month earnings per share, which compares to 21.24x for the Zacks sub-industry, 16.8x for the Zacks sector and 19.53x for the S&P 500 index.

Over the past five years, the stock has traded as high as 31.5x and as low as 8.32x, with a 5-year median of 20.63x. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$21 price target reflects 8.49x forward 12-month earnings per share.

The table below shows summary valuation data for FLS.

Valuation Multiples - FLS					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	10.04	21.24	16.8	19.53
	5-Year High	31.5	23.5	19.93	19.53
	5-Year Low	8.32	15.6	12.55	15.19
	5-Year Median	20.63	19.42	16.65	17.45
EV/EBITDA F12M	Current	7.17	10.89	16.39	12.29
	5-Year High	15.18	11.34	18.05	12.65
	5-Year Low	7.17	7.64	10.56	9.09
	5-Year Median	12.11	9.68	14.07	10.82
EV/Sales F12M	Current	1.01	2.41	2.31	2.59
	5-Year High	2.13	3.28	3.12	3.52
	5-Year Low	1.01	1.81	1.76	2.3
	5-Year Median	1.79	2.58	2.29	2.81

As of 04/20/2020

Industry Analysis Zacks Industry Rank: Bottom 22% (197 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Colfax Corporation (CFX)	Neutral	3
GEA GROUP AG SP (GEAGY)	Neutral	3
IDEX Corporation (IEX)	Neutral	4
The Middleby Corporation (MIDD)	Neutral	3
Metso Corp. (MXCYY)	Neutral	3
Roper Technologies, Inc. (ROP)	Neutral	3
Applied Industrial Technologies, Inc. (AIT)	Underperform	4
Xylem Inc. (XYL)	Underperform	4

Industry Comparison Industry: Manufacturing - General Industrial				Industry Peers		
	FLS	X Industry	S&P 500	AIT	CFX	MXCYY
Zacks Recommendation (Long Term)	Underperform	-	-	Underperform	Neutral	Neutral
Zacks Rank (Short Term)	5	-	-	4	3	3
VGM Score	C	-	-	A	D	D
Market Cap	3.23 B	1.05 B	19.37 B	1.80 B	2.75 B	3.70 B
# of Analysts	8	2	14	2	9	1
Dividend Yield	3.22%	0.00%	2.23%	2.74%	0.00%	0.00%
Value Score	C	-	-	B	B	B
Cash/Price	0.21	0.08	0.05	0.07	0.04	0.02
EV/EBITDA	8.13	9.59	11.66	7.69	12.46	18.96
PEG Ratio	0.87	2.19	2.20	NA	NA	NA
Price/Book (P/B)	1.79	1.56	2.61	1.87	0.78	2.16
Price/Cash Flow (P/CF)	8.24	8.11	10.30	6.70	5.01	21.83
P/E (F1)	13.60	15.10	17.85	13.06	16.15	13.98
Price/Sales (P/S)	0.82	0.92	2.04	0.52	0.75	1.16
Earnings Yield	7.09%	6.39%	5.48%	7.66%	6.20%	7.15%
Debt/Equity	0.84	0.50	0.71	0.91	0.69	0.05
Cash Flow (\$/share)	3.01	2.74	7.01	6.96	4.64	0.28
Growth Score	B	-	-	B	D	F
Hist. EPS Growth (3-5 yrs)	-14.64%	7.97%	10.92%	13.61%	6.78%	-4.58%
Proj. EPS Growth (F1/F0)	-20.00%	-14.38%	-3.67%	-19.05%	-38.24%	238.46%
Curr. Cash Flow Growth	15.12%	1.78%	5.93%	35.35%	27.59%	-50.28%
Hist. Cash Flow Growth (3-5 yrs)	-8.93%	4.95%	8.55%	13.96%	3.20%	-11.69%
Current Ratio	2.25	2.04	1.24	2.72	1.64	2.19
Debt/Capital	45.52%	33.54%	42.83%	47.61%	40.96%	4.57%
Net Margin	6.43%	6.43%	11.64%	3.85%	-14.45%	10.61%
Return on Equity	16.44%	11.14%	16.74%	17.79%	9.12%	16.42%
Sales/Assets	0.82	0.77	0.54	1.46	0.39	0.76
Proj. Sales Growth (F1/F0)	-7.05%	-5.41%	-0.39%	-5.41%	-16.88%	0.00%
Momentum Score	C	-	-	A	F	C
Daily Price Chg	0.08%	-1.12%	-2.18%	-0.79%	-0.13%	-0.65%
1 Week Price Chg	-8.79%	0.00%	0.42%	-9.60%	1.53%	0.49%
4 Week Price Chg	29.00%	19.30%	26.24%	28.74%	54.93%	27.07%
12 Week Price Chg	-47.34%	-27.19%	-20.02%	-27.48%	-35.55%	-33.73%
52 Week Price Chg	-50.23%	-30.08%	-12.49%	-25.55%	-23.10%	-33.94%
20 Day Average Volume	1,855,436	58,596	3,036,163	231,386	1,818,842	2,572
(F1) EPS Est 1 week change	-3.45%	0.00%	-0.14%	0.00%	-2.19%	0.00%
(F1) EPS Est 4 week change	-22.98%	-16.23%	-6.66%	-16.98%	-29.24%	-13.73%
(F1) EPS Est 12 week change	-28.46%	-19.95%	-10.02%	-18.21%	-34.43%	-27.87%
(Q1) EPS Est Mthly Chg	-32.18%	-33.29%	-9.67%	-52.08%	-75.23%	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	C
Growth Score	B
Momentum Score	C
VGM Score	C

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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