

Hexcel Corporation (HXL)

\$28.49 (As of 05/07/20)

Price Target (6-12 Months): **\$24.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 05/05/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:F

Value: F

Growth: F

Momentum: A

Summary

The rapid spread of coronavirus across the globe caused a notable decline in air travel, thereby hurting Hexcel. The outbreak forced the company to terminate its pending merger deal with Woodward and temporarily suspend its dividend payout and share buyback programs. It has also temporarily suspended its quarterly dividend payouts and share buyback program. The grounding and subsequent production halt of Boeing 737 Max is also taking a toll on this stock's growth trajectory. Evidently, the company's Engineered Product segment, which comprises Hexcel's structures and engineered core businesses, suffered a decline in its operating margin. Hexcel's shares have underperformed its industry in the past year. Nevertheless, a strong balance sheet is expected to shield the company from incurring heavy loss.

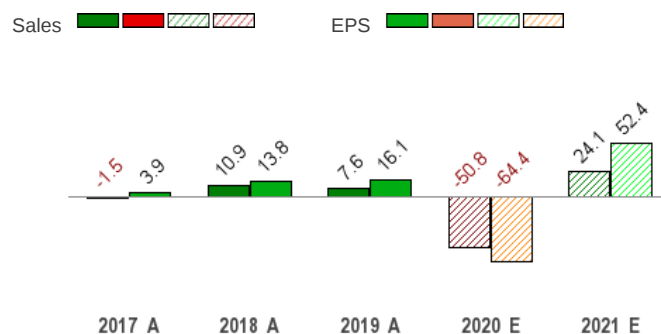
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$87.00 - \$26.69
20 Day Average Volume (sh)	1,857,233
Market Cap	\$2.4 B
YTD Price Change	-61.1%
Beta	1.22
Dividend / Div Yld	\$0.68 / 2.4%
Industry	Aerospace - Defense Equipment
Zacks Industry Rank	Bottom 13% (220 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-4.5%
Last Sales Surprise	3.3%
EPS F1 Est- 4 week change	-54.2%
Expected Report Date	07/27/2020
Earnings ESP	0.0%
P/E TTM	8.5
P/E F1	22.6
PEG F1	2.3
P/S TTM	1.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					1,437 E
2020	541 A	196 E	189 E	232 E	1,158 E
2019	610 A	609 A	573 A	564 A	2,356 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$1.92 E
2020	\$0.64 A	\$0.14 E	-\$0.01 E	\$0.07 E	\$1.26 E
2019	\$0.84 A	\$0.94 A	\$0.90 A	\$0.86 A	\$3.54 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 05/07/2020. The reports text is as of 05/08/2020.

Overview

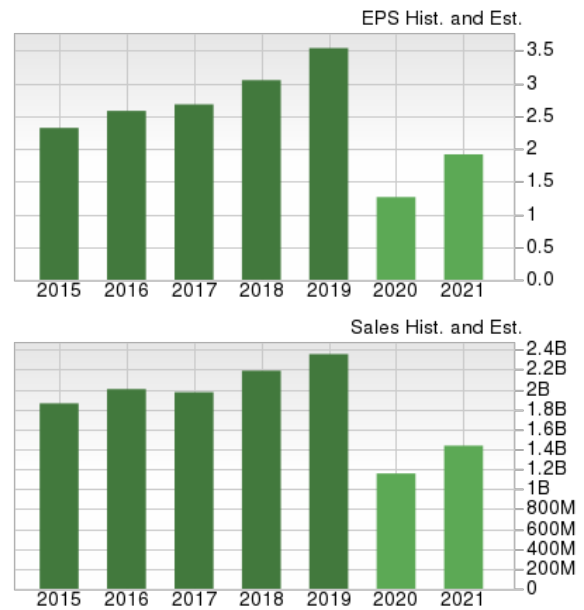
Delaware-based Hexcel Corporation develops, manufactures and distributes lightweight, high-performance structural materials for use in Commercial Aerospace, Space & Defense and Industrial markets. Hexcel Corporation, founded in 1946, was incorporated in California in 1948, and reincorporated in Delaware in 1983. The company's products are used in a wide variety of end applications, such as commercial and military aircraft, space launch vehicles and satellites, wind turbine blades, automotive and other complex industrial applications. The company serves international markets through manufacturing facilities located in the United States, Asia Pacific, Europe, Russia and Africa.

Hexcel Corporation operates in two segments namely the Composite Materials and Engineered Products.

The **Composite Materials** segment manufactures and markets carbon fibers, fabrics and specialty reinforcements, prepregs and other fiber-reinforced matrix materials, structural adhesives, honeycomb, molding compounds, tooling materials, polyurethane systems and laminates that are incorporated into military and commercial aircrafts, wind turbine blades, recreational products, automobiles and other industrial applications. Net sales for this segment were \$1,946.5 million in 2019, representing 82.6% of the company's total sales.

The **Engineered Products** segment manufactures and markets composite structures and precision machined honeycomb parts primarily for use in the aerospace industry. Composite structures are manufactured from a variety of composite and other materials, including prepregs, honeycomb, and structural adhesives, using manufacturing processes like autoclave processing, multi-axis numerically controlled machining, heat forming, and other composite manufacturing techniques. Net sales for this segment were \$493.4 million in 2019, representing 20.9% of the company's total sales.

However, total sales included corporate expenses of \$84.2 million.



Reasons To Sell:

- ▼ Lower deliveries for Boeing's 737 jets continued during the fourth quarter of 2019, following the grounding of these jets since last March. Boeing announced a temporary production rate decrease to 42 planes per month in April from 52 produced before. In December, Boeing announced its decision to temporarily suspend the production of its once fastest-selling jet. Such consecutive setbacks in the 737 Max program has affected its parts suppliers like Hexcel.

Evidently, the company's Engineered Product segment, which comprises Hexcel's structures and engineered core businesses, generated an operating income margin of 6.3% in first quarter of 2020, reflecting an annual decline of 580 basis points. This lower margin can be attributed to the 737 MAX production halt. Moreover, the company's commercial aerospace sales suffered an annual revenue loss of 12.7% in the reported quarter, with lower sales from 737 Max being the largest contributor.

- ▼ Owing to the rapid spread of coronavirus across the globe, dramatic decline in air travel along with stringent restrictions on businesses has led to significant declines in demand both within the aerospace and industrial markets. Consequently Hexcel announced dismal quarterly figures with the continued grounding of the Boeing 737 MAX and effects of the COVID-19 pandemic being the major growth inhibitors. In fact, the pandemic forced temporary closures at a number of the company's plants as well as customer plants, which led to reduced sales. The company was also forced to temporarily suspend its quarterly dividend payouts, share buyback program as well as withdrew its 2020 guidance.

The pandemic's impact has been so immense that Hexcel had to mutually terminate its pending merger deal worth \$6.4 billion with Woodward. Notably, synergies from the combination of these two companies might have not brought out the desired results in the current scenario.

- ▼ International Air Transport Association (IATA) estimates in its latest report that 2020 may witness a 55% annual decline in global airline passenger revenues. This poses a serious threat to growth of aircraft manufacturing stocks along with those that supply parts like Hexcel. The fact that the company is already feeling the heat of the outbreak indicates the risk to the stock. This may have led the company's shares to decline 59.4% compared with the industry's decline of 42.1% in the past year.

737 Max issue and effects of the coronavirus pandemic poses concern for Hexcel Corp.'s growth

Risks

- To compete in the diverse industries in which the company caters to, Hexcel Corp. continues to collaborate with companies in innovating new products, to capture larger market shares. In February 2020, Hexcel Corp. collaborated with NaCa Systems, a Tier 1 supplier of natural fiber composite automotive interior parts, on the development of a lightweight carbon fiber prepreg and wood fiber composite sports car seat back using a rapid press molding process. This innovation validates a short-cycle time production process for CFRP and wood fiber composite parts and offers a host of benefits to automotive manufacturers. Further, this April, Hexcel Corp. announced the launch of its new low temperature fast cure HexBond 679 adhesive film, which is designed to deliver robust bonding performance in sandwich structures and offers significant cycle time reductions with its short-cure cycles at low temperatures. Such innovations should bolster this stock's growth over the long run.
- Hexcel ended the first quarter of 2020 with cash and cash equivalents of \$329.3 million compared with \$64.4 million as of Dec 31, 2019. The company's long-term debt of \$1,390 million as of Mar 31, 2020, came in higher than \$1,051 million as of Dec 31, 2019. Although the company's long-term debt remains much higher than the cash reserve, its current debt worth \$1.2 million lies much lower than the cash balance. So, this is good news for the company's solvency level at least in the near term.

Moreover, the company's current ratio of 3.36 as of Mar 31, 2020, is up sequentially from 2.19 as of Dec 31, 2019. This also encourages us, further considering the fact that a current ratio of more than 1 indicates the company's capability to pay off its short-term obligations. Moreover, to cope with the impact of the virus outbreak, Hexcel has started implementing significant reductions in its U.S. workforce, as well as short-term cost savings actions, including temporary salary reductions, unpaid furloughs, and suspension of employee stock purchase plan. We expect such initiatives to shield the company from a loss, at least in the near term.

Last Earnings Report

Hexcel Misses on Q1 Earnings, Withdraws 2020 View

Hexcel reported first-quarter 2020 adjusted earnings of 64 cents per share, which missed the Zacks Consensus Estimate of 67 cents by 4.5%.

In the reported quarter, the company's GAAP earnings came in at 50cents compared with the prior-year quarter's 84 cents.

The year-over-year deterioration can be attributed to the continued grounding of the Boeing 737 MAX and effects of the COVID-19 pandemic.

Quarter Ending 03/2020

Report Date	Apr 20, 2020
Sales Surprise	3.34%
EPS Surprise	-4.48%
Quarterly EPS	0.64
Annual EPS (TTM)	3.34

Total Sales

Net sales totaled \$541 million, surpassing the Zacks Consensus Estimate of \$524 million by 3.3%. However, the top line witnessed a decline of 11.3% from the year-ago quarter's \$609.9 million.

While stalled production of 737 Max affected sales, temporary closures at a number of Hexcel's plants as well as customer plants led by the pandemic resulted in reduced quarterly sales.

Operational Update

Hexcel's gross margin was 26% in the first quarter, reflecting year-over-year contraction of 140 basis points.

The company's operating income amounted to \$65.7 million in the quarter compared with the previous year's \$102.8 million. The deterioration was mainly caused by non-recurring advisory and professional fees and expenses that the company incurred on account of its recently terminated merger with Woodward.

Quarterly Performance

Commercial Aerospace: Net sales were down 12.7% year over year to \$362.9 million. The grounding and subsequent production halt of 737 Max and end of the A380 program resulted in this unit's poor top-line performance.

Space and Defense: Net sales rose 3.5% year over year to \$111.6 million, primarily driven by improved sales from rotorcraft, particularly the Black Hawk program, and a number of Space programs.

Industrial: Net sales declined 23.2% year over year to \$66.5 million, primarily due to soft wind energy sales on account of temporary plant closures in China and Austria arising from the COVID-19 pandemic.

Financial Details

As of Mar 31, 2020, cash and cash equivalents were \$329.3 million compared with \$64.4 million as of Dec 31, 2019.

Long-term debt totaled \$1,389.5 million as of Mar 31, 2020, up from \$1,050.6 million as of 2019-end.

At the end of first-quarter 2020, cash generated from operating activities was \$8.6 million compared with \$45.9 million in the prior year.

The effective tax rate for the firstquarter of 2020 was 21.9% compared with 22.7% in the year-ago period. The firstquarter of 2020 was favorably impacted by deductions associated with share-based compensation payments.

The company used \$25 million to repurchase shares of its common stock during the first quarter. The remaining authorization under the share repurchase program as of Mar 31, 2020 was \$217million. However, Hexcel has temporarily suspended its share repurchase program and quarterly dividend payouts, in light of the current market volatility.

Free cash outflow for the first quarter of 2020 was \$18.6 million compared with \$15.2 million in the first quarter of 2019.

2020 Guidance

Hexcel has withdrawn its previously provided 2020 and mid-term financial guidance due to market uncertainties as a result of the pandemic.

Recent News

On **Apr 6, 2020**, Hexcel Corporation and Woodward announced that the companies have mutually agreed to terminate their merger agreement, previously announced on January 12, 2020, under which the parties had agreed to combine in an all-stock merger of equals.

The termination was approved by the Boards of Directors of both companies and is in response to the increasing impact on both the aerospace and industrial sectors, and global markets broadly, resulting from the health crisis caused by the coronavirus (COVID-19) pandemic. The pandemic has resulted in a need for each company to focus on its respective businesses and has impacted the companies' ability to realize the benefits of the merger during these unprecedented times.

Valuation

Hexcel Corp.'s shares are down 61% in the year to date period and 59.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are down 48.5% and 35.6% in the year to date period, respectively. Over the past year, the Zacks sub-industry and sector are down 42.1% and 32.3%, respectively.

The S&P 500 index is down 9.8% in the year to date period and up 2.3% in the past year.

The stock is currently trading at 19.1X forward 12-month earnings, which compares to 19X for the Zacks sub-industry, 19X for the Zacks sector and 20.8X for the S&P 500 index.

Over the past five years, the stock has traded as high as 23.5X and as low as 8.1X, with a 5-year median of 19.1X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$24 price target reflects 16.1X forward 12-month earnings.

The table below shows summary valuation data for HXL

Valuation Multiples - HXL					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	19.09	18.99	19.03	20.81
	5-Year High	23.52	19.86	20.94	20.81
	5-Year Low	8.06	12.99	14.17	15.19
	5-Year Median	19.1	17.1	17.06	17.44
P/S F12M	Current	1.89	0.72	1.04	3.23
	5-Year High	2.91	1.29	1.49	3.44
	5-Year Low	1.01	0.72	0.92	2.54
	5-Year Median	2.33	1.03	1.18	3.01
EV/EBITDA TTM	Current	6.39	6.76	9.95	10.51
	5-Year High	16.69	12.02	14.98	12.86
	5-Year Low	6.16	6.27	7.39	8.28
	5-Year Median	13.02	8.77	10.42	10.77

As of 05/07/2020

Industry Analysis Zacks Industry Rank: Bottom 13% (220 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
AAR Corp (AIR)	Neutral	3
Aerojet Rocketdyne Holdings Inc (AJRD)	Neutral	4
Astronics Corporation (ATRO)	Neutral	3
CurtissWright Corporation (CW)	Neutral	3
Heico Corporation (HEI)	Neutral	4
Leidos Holdings Inc (LDOS)	Neutral	2
Spirit Aerosystems Holdings Inc (SPR)	Neutral	3
Teledyne Technologies Incorporated (TDY)	Neutral	3

Industry Comparison Industry: Aerospace - Defense Equipment				Industry Peers		
	HXL	X Industry	S&P 500	AJRD	ATRO	TDY
Zacks Recommendation (Long Term)	Underperform	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	5	-	-	4	3	3
VGM Score	F	-	-	F	B	D
Market Cap	2.38 B	1.01 B	19.51 B	3.15 B	245.45 M	11.74 B
# of Analysts	3	3	14	2	1	1
Dividend Yield	2.39%	0.00%	2.15%	0.00%	0.00%	0.00%
Value Score	F	-	-	F	B	F
Cash/Price	0.12	0.11	0.06	0.28	0.12	0.02
EV/EBITDA	6.06	6.90	11.77	8.46	3.74	20.40
PEG Ratio	2.34	3.31	2.54	NA	NA	NA
Price/Book (P/B)	1.67	1.65	2.67	5.11	0.64	4.26
Price/Cash Flow (P/CF)	5.39	6.27	10.44	14.75	3.95	23.08
P/E (F1)	23.31	18.01	19.30	22.80	NA	34.43
Price/Sales (P/S)	1.04	0.64	1.99	1.60	0.34	3.67
Earnings Yield	4.42%	4.42%	4.91%	4.39%	-11.76%	2.90%
Debt/Equity	0.98	0.35	0.75	0.63	0.48	0.31
Cash Flow (\$/share)	5.29	2.02	7.01	2.72	2.02	13.88
Growth Score	F	-	-	F	B	B
Hist. EPS Growth (3-5 yrs)	10.08%	13.43%	10.87%	37.62%	-20.14%	18.64%
Proj. EPS Growth (F1/F0)	-64.31%	-16.99%	-9.87%	4.14%	-203.30%	-11.51%
Curr. Cash Flow Growth	12.73%	9.60%	5.88%	-8.04%	-23.43%	14.47%
Hist. Cash Flow Growth (3-5 yrs)	9.27%	4.37%	8.55%	70.16%	-8.28%	11.00%
Current Ratio	3.36	2.39	1.24	1.67	2.84	1.80
Debt/Capital	49.44%	31.14%	44.23%	38.69%	32.59%	23.89%
Net Margin	12.10%	5.34%	10.68%	6.80%	-12.89%	12.78%
Return on Equity	19.92%	8.64%	16.36%	21.60%	3.26%	15.49%
Sales/Assets	0.71	0.74	0.55	0.74	0.93	0.72
Proj. Sales Growth (F1/F0)	-50.86%	0.00%	-2.26%	3.33%	-31.59%	0.13%
Momentum Score	A	-	-	C	C	D
Daily Price Chg	2.96%	0.67%	1.52%	0.45%	11.90%	1.06%
1 Week Price Chg	12.45%	4.42%	0.53%	-1.94%	10.53%	1.20%
4 Week Price Chg	-19.57%	-5.82%	0.73%	-7.75%	-16.51%	-2.34%
12 Week Price Chg	-62.07%	-33.05%	-21.09%	-27.71%	-68.62%	-18.31%
52 Week Price Chg	-59.64%	-32.53%	-10.17%	5.89%	-79.86%	29.19%
20 Day Average Volume	1,857,233	184,180	2,398,409	594,066	340,595	217,083
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-1.95%	0.00%	0.00%
(F1) EPS Est 4 week change	-54.17%	-6.52%	-6.95%	-9.04%	-66.67%	-4.50%
(F1) EPS Est 12 week change	-66.22%	-26.87%	-15.68%	-12.98%	-174.66%	-16.50%
(Q1) EPS Est Mthly Chg	-12.50%	-12.30%	-13.12%	-8.27%	NA	25.16%

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	F
Growth Score	F
Momentum Score	A
VGM Score	F

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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