

Lincoln Electric (LECO)

\$76.61 (As of 05/07/20)

Price Target (6-12 Months): **\$66.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 04/30/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:F

Value: F

Growth: D

Momentum: D

Summary

Lincoln Electric's first-quarter 2020 adjusted earnings came in-line with the Zacks Consensus Estimate while sales missed the same. The company's top and bottom lines both declined year over year due to weak demand. The COVID-19 pandemic has impacted Lincoln Electric's markets and operations, weakening demand, leading to supply chain disruptions, and other logistics constraints. In April, global demand trends were reported to have declined in the low 40% range compared with the prior year. Consequently, second-quarter results are likely to reflect this trend. In addition to weak demand, increase in customer facility closures and the continued risk of possible supply chain disruptions are anticipated to result in lower operating activity and higher inefficiencies in the business. and will impact results.

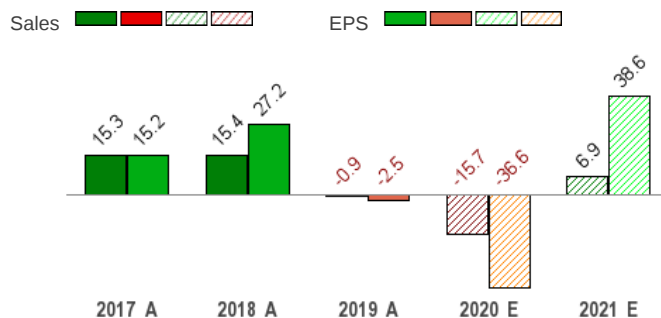
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$98.32 - \$59.30
20 Day Average Volume (sh)	329,316
Market Cap	\$4.5 B
YTD Price Change	-20.8%
Beta	1.25
Dividend / Div Yld	\$1.96 / 2.6%
Industry	Manufacturing - Tools & Related Products
Zacks Industry Rank	Bottom 6% (238 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	0.0%
Last Sales Surprise	-1.4%
EPS F1 Est- 4 week change	-19.9%
Expected Report Date	07/28/2020
Earnings ESP	-9.3%
P/E TTM	17.0
P/E F1	25.7
PEG F1	2.3
P/S TTM	1.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	698 E	645 E	631 E	697 E	2,705 E
2020	702 A	549 E	601 E	679 E	2,531 E
2019	759 A	777 A	731 A	736 A	3,003 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.18 E	\$0.98 E	\$0.93 E	\$1.07 E	\$4.13 E
2020	\$1.00 A	\$0.29 E	\$0.71 E	\$0.98 E	\$2.98 E
2019	\$1.17 A	\$1.28 A	\$1.09 A	\$1.15 A	\$4.70 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

Headquartered in Cleveland, OH, Lincoln Electric has more than 59 manufacturing locations, including operations and joint ventures in 18 countries, and a worldwide network of distributors and sales offices covering more than 160 countries.

Lincoln is a full-line manufacturer and reseller of welding and cutting products with products ranging from welding power sources, wire feeding systems, robotic welding packages, fume extraction equipment, consumables and fluxes to regulators and torches used in cutting.

Lincoln Electric produces three types of arc welding electrodes, including stick electrodes, solid electrodes used for continuous feeding in mechanized welding, and cored electrodes that are also used for mechanized welding. Arc welding is carried out in many industries. The metal working field involves production of arc welding in transportation, construction, fabrication, petrochemical and other industries.

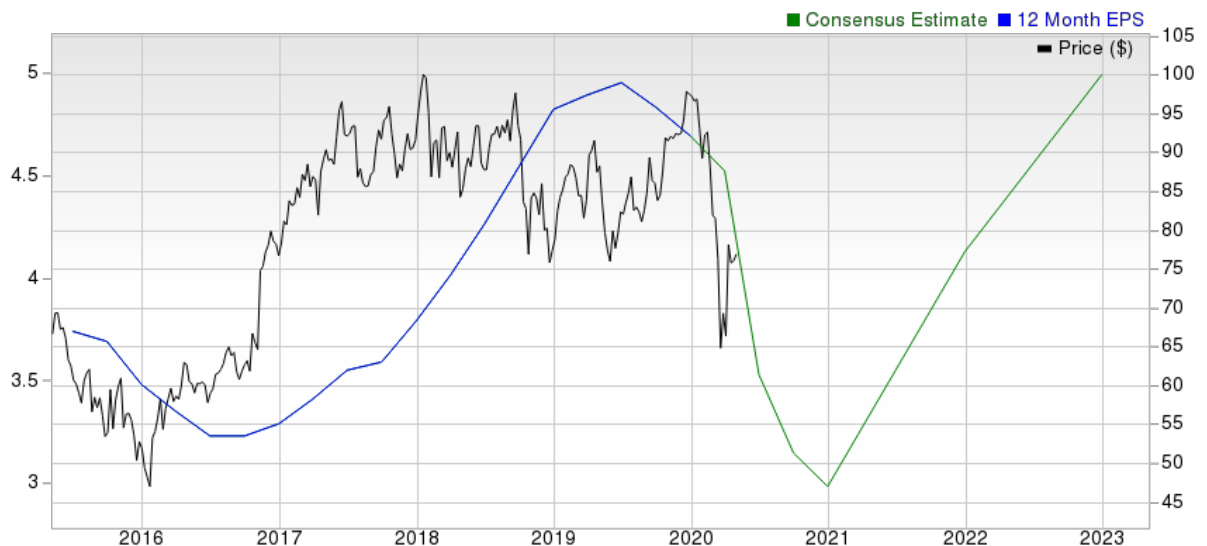
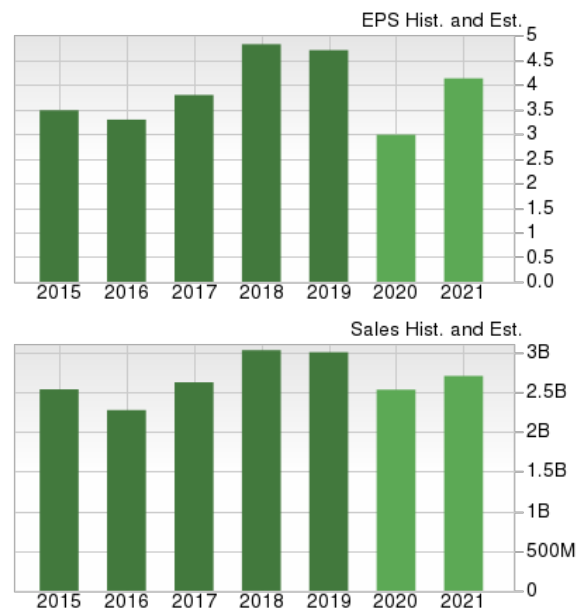
The company's business units are aligned into three operating segments-

The **Americas Welding** segment (62% of fiscal 2019 revenues) includes welding operations in North and South America.

The **International Welding** (28% of fiscal 2019 revenues) segment includes welding operations in Europe, Africa, Asia and Australia.

The **Harris Products Group** (11% of fiscal 2019 revenues) includes the company's global cutting, soldering and brazing businesses, and retail business in the United States.

During April 2019, the company acquired Detroit, MI-based Baker Industries, a provider of custom tooling, parts and fixtures primarily serving automotive and aerospace markets. During December 2018, the company acquired the soldering business of Worthington Industries, which broadens Harris Products Group's portfolio of industry-leading consumables. Further during December 2018, the company acquired Coldwater Machine Company and Pro System to accelerate growth and expand the company's industry-leading portfolio of automated cutting and joining solutions. Moreover during December 2018, the company acquired Ontario, Canada-based Inovatech Engineering Corporation which scales the company's automated cutting solutions and application expertise and supports long-term growth in that market.



Reasons To Sell:

- ▼ The COVID-19 pandemic has impacted Lincoln Electric's markets and operations, which include weakening demand, supply chain disruptions, and other logistics constraints. Automotive, transportation, energy, construction and heavy industries have all been impacted. The company also stated that global demand trends weakened significantly in April, declining in the low 40% range compared with the prior year. Consequently, the company expects a more challenging second quarter. In addition to weak demand, increase in customer facility closures and the continued risk of possible supply chain disruptions are expected to result in lower operating activity and higher inefficiencies in the business.
- ▼ Lincoln Electric's Americas Welding segment has been bearing the brunt of a weak manufacturing sector thanks to the U.S.-China trade tensions. The coronavirus pandemic has dealt a further blow to the sector. Per the Federal Reserve, industrial production contracted 7.5% in first-quarter 2020 — the steepest since second-quarter 2009. Manufacturing output also slumped at an annual rate of 7.1% in the first quarter, the sharpest since first-quarter 2009. Meanwhile, per the Institute for Supply Management, the Manufacturing Purchasing Managers' Index (PMI) after recording 50.9 in January, and 50.1 in February (indicating expansion), contracted again to 49.1% in March. Thus, a weak manufacturing backdrop, uncertainty in the market and cautious customer spending are likely to persist this year aggravated by the coronavirus outbreak. This remains a concern for Lincoln Electric.
- ▼ Pricing declined 0.9% in first-quarter 2020, reflecting the removal of surcharges in the U.S. business and is expected to be lower in second-quarter 2020. Raw material inflation will remain a headwind in 2020. Even though the company continues to announce new pricing actions, incremental margins could be impacted due to the timing of its response. Given its focus on innovation as a key value proposition, Lincoln Electric continued to increase investment in product development with higher year-over-year R&D spending. Though this has long-term benefits, it will impede margins in the near term. Also, a stronger U.S. dollar will affect the company's exports.
- ▼ Lincoln Electric recognized \$6.5 million in pre-tax rationalization charges in first-quarter 2020. These charges are primarily related to employee severance, asset impairments and gains or losses on the disposal of assets. The company expects an additional \$10 to \$15 million in charges in 2020.

Lincoln Electric's volumes will continue to bear the brunt of the ongoing slowdown in industrial production and the impact of the COVID-19 pandemic on its demand and supply chain.

Risks

- As of Mar 31, 2020, Lincoln Electric had liquidity of \$477 million comprising \$163 million in cash and \$314 million in available credit under existing borrowing facilities. Total debt as of Mar 31, 2020 was at \$848 million, up from \$705 million as of Mar 31, 2019, primarily due to additional short-term borrowings. Its first long-term debt maturity is due in August 2025. Lincoln Electric's total debt to total capital ratio as of Mar 31, 2020 was at 0.56. The company's times interest earned ratio is 15.9, much higher than the industry's 5.3. This indicates that the company is poised well to navigate through this challenging period.
 - The company is focusing on cost management to sustain margins in the backdrop of weak demand. These measures include reduced work hours, overtime, lowering headcount, deferring annual wage increases and freezing hiring. The company has also cut down discretionary spending and eliminated travel. It has commenced three manufacturing facility rationalizations to align with demand. The company is evaluating additional contingency measures, which will be implemented if the situation demands. Lincoln Electric anticipates these new measures and earlier actions to now generate \$40 to \$45 million in realized cost savings in 2020 and permanent cost savings per quarter of \$6 million and \$7 million, thereafter.
 - The company is focused on new product development and using digital platforms to engage customers. Lincoln Electric's product launches in the automation solutions market are likely to aid growth. The company is focused on its new additive services business, which will position Lincoln Electric as a manufacturer of large scale 3D-printed metal parts, prototypes and tooling for industrial customers. This is likely to be growth opportunity for Lincoln Electric. It also continues to invest in long-term strategy for automation in support of its 2020 strategy initiatives. The company launched its new state-of-the-art advanced technology solution center in Germany, which gives it an unprecedented commercial presence in the European market. This tech center will enable the company to showcase its latest technologies and welding consumables, equipment and automation.
 - Lincoln Electric is benefiting from several acquisitions. Lincoln Electric has acquired Inovatech Engineering Corporation and Coldwater Machine Company, Pro Systems LLC, boosting its automated cutting solutions and application expertise. In January 2019, Lincoln Electric acquired the soldering business of Worthington Industries. This broadened the Harris Products Group's portfolio of industry-leading consumables with the addition of premium solders and fluxes. In April 2019, Lincoln Electric acquired Baker Industries to expand automation and additive strategies. Recently, the company acquired an controlling interest in Askaynak, a leading Turkish producer of welding consumables and equipment. The buyout advances the company's regional growth strategy in Europe, the Middle East and Africa.
 - Lincoln Electric has a balanced capital allocation strategy, prioritizing capital investment spending to cost reduction, new products, and growth initiatives. It has reduced its planned capital expenditure for 2020 by approximately 15% to a range of \$55-\$65 million. The company will continue to evaluate M&A options focused primarily on tuck-in assets. It is maintaining dividend program but has temporarily suspended share repurchases. Lincoln Electric plans to resume repurchases as business conditions improve.
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Last Earnings Report

Lincoln Electric Q1 Earnings Match, Sales Lag Estimates

Lincoln Electric reported first-quarter 2020 adjusted earnings of \$1.00 per share, which matched the Zacks Consensus Estimate. However, the reported figure declined around 15% year over year. The company witnessed low demand owing to the COVID-19 pandemic, which dealt a blow to an already ailing industrial sector.

Including one-time items, the bottom line came in at 91 cents compared with \$1.12 in the prior-year quarter.

Total revenues declined 7.5% year over year to \$702 million. This can be attributed to a decrease of 9.5% in organic sales and an unfavorable impact of 1.3% from foreign exchange, which offset a gain of 3.2% from acquisitions. Further, the top line missed the Zacks Consensus Estimate of \$712 million.

Costs and Margins

Cost of goods sold was down 7% to \$465 million from \$501 million in the prior-year quarter. Gross profit declined 8% to \$237 million from the prior-year quarter figure of \$258 million. Gross margin came in at 33.8% compared with 34.0% in the year-ago quarter.

Selling, general and administrative expenses declined 7% year over year to \$150 million from the prior-year quarter. Adjusted operating profit was down 11% year over year to \$88.4 million in the quarter. Adjusted operating margin came in at 12.6% compared with 13.0% in the year-ago quarter.

Financial Update

Lincoln Electric had cash and cash equivalents of around \$163 million at the end of first-quarter 2020 compared with \$200 million at the end of the 2019. The company reported record cash flow from operations of \$22 million during the first quarter compared with \$26 million in the prior-year quarter. The company's debt to invested capital was at 55.9% at the end of first-quarter 2020 compared with 47.7% as of the end of fiscal 2019.

During first-quarter 2020, Lincoln Electric returned \$140 million to shareholders through dividend and share repurchases.

Outlook

The company cautioned that global demand trends are at weak levels currently. To counter this impact, the company has expanded its cost reduction initiatives to sustain margins in the backdrop. These actions are anticipated to contribute approximately \$40 million to \$45 million of annualized cost savings in 2020.

Quarter Ending 03/2020

Report Date	Apr 27, 2020
Sales Surprise	-1.37%
EPS Surprise	0.00%
Quarterly EPS	1.00
Annual EPS (TTM)	4.52

Valuation

Lincoln Electric's shares are down 6.6% over the trailing 12-month period. Stocks in the Zacks Manufacturing – Tool & Related Products industry and the Zacks Industrial Products sector are down 22.1% and 18.2% over the past year, respectively.

The S&P 500 index has gained 0.2% in the past year.

The stock is currently trading at 22.63X forward 12-month earnings, which compares with 19.49X for the Zacks sub-industry, 18.50X for the Zacks sector and 20.81X for the S&P 500 index.

Over the past five years, the stock has traded as high as 25.36X and as low as 12.33X, with a 5-year median of 17.68X.

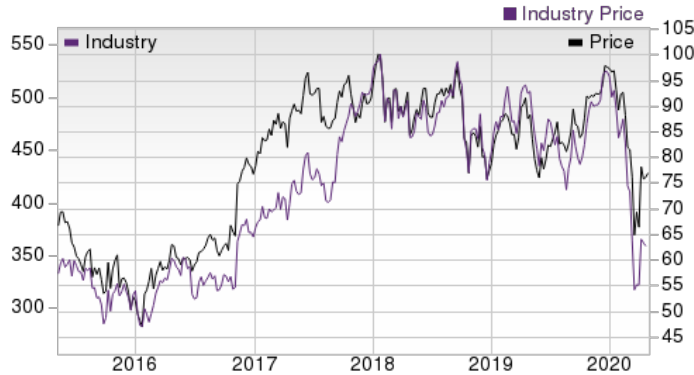
Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$66 price target reflects 19.50X Forward 12-month earnings.

The table below shows summary valuation data for LECO:

Valuation Multiples - LECO					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	22.63	19.49	18.5	20.81
	5-Year High	25.36	20.19	19.93	20.81
	5-Year Low	12.33	12.36	12.55	15.19
	5-Year Median	17.68	16.39	16.56	17.44
P/S F12M	Current	1.76	1.1	2.41	3.25
	5-Year High	2.6	1.52	2.72	3.44
	5-Year Low	1.2	0.84	1.52	2.54
	5-Year Median	1.8	1.18	1.99	3.01
EV/EBITDA TTM	Current	11.78	8.27	13.71	10.57
	5-Year High	23.58	12.99	17.4	12.86
	5-Year Low	8.17	6.22	10.8	8.28
	5-Year Median	13.69	9.88	14.7	10.77

As of 05/07/2020

Industry Analysis Zacks Industry Rank: Bottom 6% (238 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
DeereCompany (DE)	Neutral	4
John Bean Technologies Corporation (JBT)	Neutral	4
The Manitowoc Company Inc (MTW)	Neutral	3
Sandvik AB (SDVKY)	Neutral	3
Terex Corporation (TEX)	Neutral	3
Caterpillar Inc (CAT)	Underperform	5
Kennametal Inc (KMT)	Underperform	4
Stanley BlackDecker Inc (SWK)	Underperform	4

Industry Comparison Industry: Manufacturing - Tools & Related Products				Industry Peers		
	LECO	X Industry	S&P 500	CNHI	JBT	KMT
Zacks Recommendation (Long Term)	Underperform	-	-	Neutral	Neutral	Underperform
Zacks Rank (Short Term)	5	-	-	3	4	4
VGM Score	F	-	-	B	D	C
Market Cap	4.55 B	3.28 B	19.51 B	7.30 B	2.23 B	1.90 B
# of Analysts	7	6.5	14	6	5	5
Dividend Yield	2.56%	1.76%	2.15%	0.00%	0.57%	3.49%
Value Score	F	-	-	A	D	B
Cash/Price	0.04	0.11	0.06	0.71	0.03	0.05
EV/EBITDA	10.78	9.26	11.77	7.87	11.49	5.32
PEG Ratio	2.38	3.16	2.54	NA	3.54	5.77
Price/Book (P/B)	6.81	2.27	2.67	1.29	3.91	1.46
Price/Cash Flow (P/CF)	12.46	9.41	10.44	3.06	9.90	5.20
P/E (F1)	26.20	25.67	19.30	35.28	19.55	28.83
Price/Sales (P/S)	1.54	1.18	1.99	0.27	1.12	0.90
Earnings Yield	3.89%	3.89%	4.91%	2.77%	5.11%	3.49%
Debt/Equity	1.07	0.41	0.75	4.16	1.29	0.48
Cash Flow (\$/share)	6.15	3.14	7.01	1.77	7.10	4.42
Growth Score	D	-	-	D	C	C
Hist. EPS Growth (3-5 yrs)	9.32%	9.32%	10.87%	23.49%	28.53%	17.42%
Proj. EPS Growth (F1/F0)	-36.50%	-36.19%	-9.87%	-81.75%	-27.54%	-73.64%
Curr. Cash Flow Growth	-3.32%	4.61%	5.88%	-1.24%	14.88%	10.92%
Hist. Cash Flow Growth (3-5 yrs)	0.03%	6.22%	8.55%	2.82%	25.60%	2.02%
Current Ratio	1.62	2.52	1.24	6.13	1.71	2.52
Debt/Capital	51.73%	29.09%	44.23%	80.61%	56.24%	32.59%
Net Margin	9.41%	6.81%	10.68%	4.06%	6.96%	3.10%
Return on Equity	35.65%	11.65%	16.36%	14.21%	30.83%	10.16%
Sales/Assets	1.25	0.76	0.55	0.59	1.04	0.81
Proj. Sales Growth (F1/F0)	-15.71%	-13.43%	-2.26%	-17.68%	-11.49%	-20.40%
Momentum Score	D	-	-	D	C	D
Daily Price Chg	1.22%	0.66%	1.52%	-2.70%	3.07%	-1.54%
1 Week Price Chg	1.13%	1.89%	0.53%	-4.15%	-1.91%	1.03%
4 Week Price Chg	-1.91%	3.50%	0.73%	-17.28%	-19.67%	-2.34%
12 Week Price Chg	-17.69%	-17.69%	-21.09%	-43.17%	-37.93%	-28.64%
52 Week Price Chg	-8.72%	-20.58%	-10.17%	-44.51%	-35.91%	-36.92%
20 Day Average Volume	329,316	46,990	2,398,409	876,998	239,977	1,068,015
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-50.54%	0.56%	-0.71%
(F1) EPS Est 4 week change	-19.90%	-19.73%	-6.95%	-68.81%	-6.55%	-19.73%
(F1) EPS Est 12 week change	-41.06%	-39.73%	-15.68%	-82.00%	-31.07%	-39.39%
(Q1) EPS Est Mthly Chg	-62.52%	-65.53%	-13.12%	-110.85%	-23.05%	-68.54%

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	D
Momentum Score	D
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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