

## Lincoln Electric (LECO)

**\$77.72** (As of 04/08/20)

Price Target (6-12 Months): **\$82.00**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Neutral**

(Since: 12/30/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**4-Sell**

Zacks Style Scores:

VGM:C

Value: D

Growth: A

Momentum: F

## Summary

Lincoln Electric's volumes in 2020 are likely to bear the brunt of slowdown in industrial production and weak automotive sector. The impact of coronavirus outbreak – lower order levels due to cautious customer spending, supply chain disruptions, impact of factory closures, is likely to get reflected in this year's results. The estimates for the first quarter and fiscal have thus undergone negative revisions lately. In this backdrop, Lincoln Electric's cost management actions, which include lower work hours, less overtime, suspension of new hiring and cutting down discretionary spending, will help sustain margins. The company is focused on innovative products and acquisitions, which is likely to drive growth. It also continues to invest in long-term strategy for automation in support of its 2020 strategy initiatives.

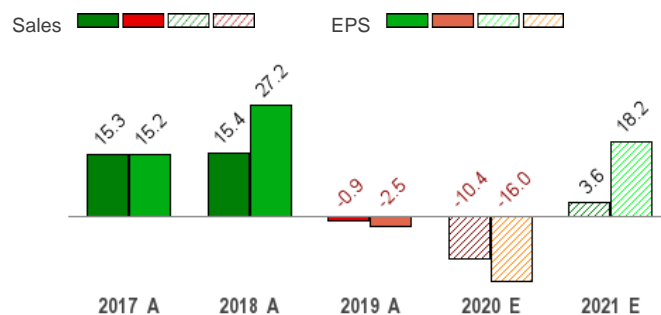
## Price, Consensus & Surprise



## Data Overview

52 Week High-Low	\$98.32 - \$59.30
20 Day Average Volume (sh)	600,410
Market Cap	\$4.7 B
YTD Price Change	-19.7%
Beta	1.24
Dividend / Div Yld	\$1.96 / 2.5%
Industry	<a href="#">Manufacturing - Tools &amp; Related Products</a>
Zacks Industry Rank	Bottom 6% (237 out of 253)

## Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	1.8%
Last Sales Surprise	-0.1%
EPS F1 Est- 4 week change	-16.2%
Expected Report Date	04/27/2020
Earnings ESP	-0.8%
P/E TTM	16.6
P/E F1	19.7
PEG F1	1.8
P/S TTM	1.6

## Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	756 E	778 E	741 E	789 E	2,787 E
2020	723 E	669 E	653 E	723 E	2,691 E
2019	759 A	777 A	731 A	736 A	3,003 A

## EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.17 E	\$1.16 E	\$1.27 E	\$1.42 E	\$4.67 E
2020	\$1.02 E	\$0.85 E	\$0.93 E	\$1.15 E	\$3.95 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 04/08/2020. The reports text is as of 04/09/2020.

## 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.

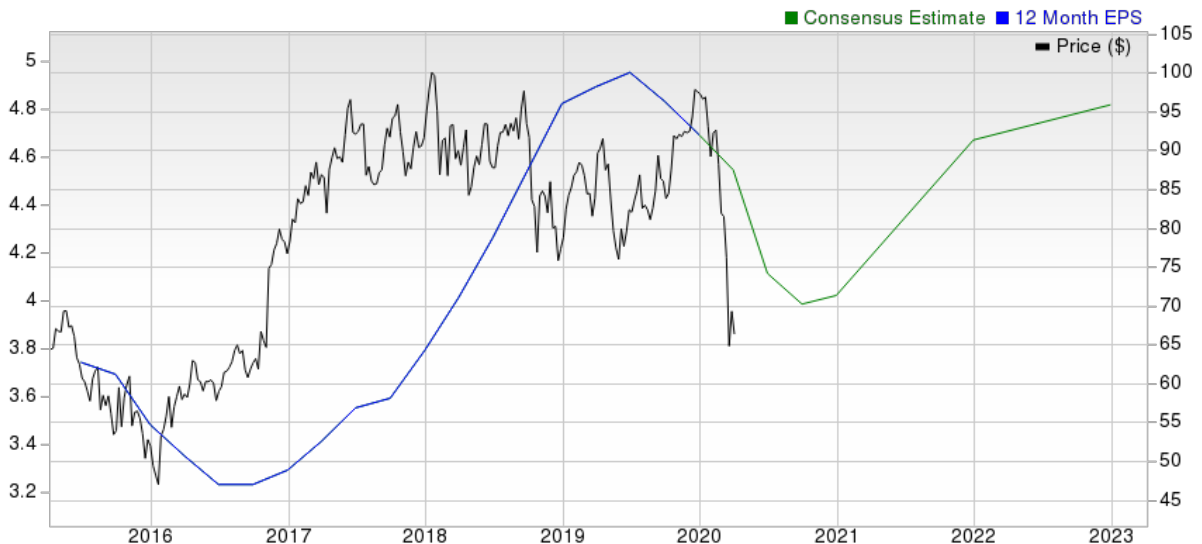
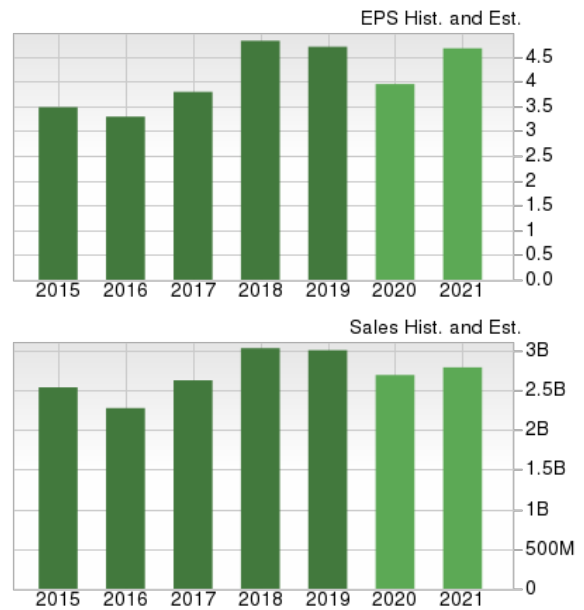
The company's business units are aligned into three operating segments-

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.



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## Reasons To Buy:

- ▲ The company is focusing on cost management to sustain margins in the backdrop of the weakness in global industrial production. The initiatives include lower work hours, less overtime, suspension of new hiring and cutting down discretionary spending. The company is now planning to freeze senior management wages. Lincoln Electric expects \$15-\$18 million of annualized cost savings. This will start from second-quarter 2020 and major part of it will be realized in the back half of 2020. The company is evaluating additional contingency measures, which will be implemented if the situation demands.
- ▲ Lincoln Electric's product launches in the automation solutions market are likely to aid growth. The company is also preparing for the launch of 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 expects to maintain a balanced capital allocation strategy, prioritizing growth investments and returning cash to shareholders through dividend program and share repurchases. Lincoln Electric generated record \$403 million of cash flow from operations in 2019 and achieved 113% cash conversion. The company returned around \$411 million to shareholders during 2019 through share repurchases and dividends. Lincoln Electric's board of director's approved a new share repurchase program authorizing the company to repurchase up to 10 million of its outstanding common stock. This authorization is in addition to the 2.8 million shares remaining from the prior program. The company's board of directors also authorized a 4.3% increase in the quarterly cash dividend – its 24th consecutive increase. It also spent \$70 million in capital expenditures in the 2019. In 2020, the company will continue to prioritize capital for both organic and inorganic growth and expects to invest \$65 million to \$75 million in capital expenditures. Despite investing for growth, the company maintains solid balance sheet and continues to deliver ROIC at 20%. It also plans to continue to repurchase shares.

Focus on acquisitions, innovative product launches and execution of the 2020 vision and strategy will drive Lincoln Electric's growth. Its cost management actions will also aid margins.

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## Reasons To Sell:

- ▼ Volumes in the Americas Welding segment continue to remain challenged thanks to the overall slowdown in industrial production and lower capital spending for automation systems. The Automotive/Transportation sector declined at a double-digit percent in fourth-quarter 2019. In the International Welding segment, volumes continue to be impacted by declines in Asia Pacific and Europe as well as lower global industrial production. Headwinds like weak global manufacturing backdrop, uncertainty in the market and cautious customer spending are likely to persist this year as well further exacerbated by the coronavirus outbreak. Lincoln Electric also anticipates headwinds from rising expected incentive compensation and projected higher tax rate in 2020 to impact earnings.
- ▼ Pricing in the Americas Welding segment declined 1.2% in third-quarter 2019 and 1.7% in the fourth quarter, reflecting the removal of surcharges in the U.S. business. The company anticipates pricing to be lower in the first half of 2020. The impact of the coronavirus outbreak is also a concern. Factory closures in China might impact Lincoln Electric's results in the ongoing quarter. The company also stands the risk of supply chain disruptions. Further, it is also weighing on customer confidence and might impact customer orders.
- ▼ 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's volumes will be hurt by slowdown in industrial production and the automotive sector. Further, the impact of the coronavirus outbreak and higher costs will weigh on results.

## Last Earnings Report

### Lincoln Electric Q4 Earnings Top, Sales Lag Estimates

Lincoln Electric Holdings reported fourth-quarter 2019 adjusted earnings of \$1.15 per share, which beat the Zacks Consensus Estimate of \$1.13. However, the reported figure declined 11% year over year. While reduction in global industrial production rates across most of the end sectors impacted demand for consumables, slowdown in capital spending and project deferrals reduced orders for automated systems. This impacted the company's fourth-quarter top and bottom-line performance.

Including one-time items, the bottom line came in at \$1.03 compared with \$1.35 in the prior-year quarter.

Total revenues declined 1% year over year to \$736 million as a decrease of 6.5% in organic sales offset a gain of 5.9% from acquisitions. The top line missed the Zacks Consensus Estimate of \$737 million.

### Costs and Margins

Cost of goods sold was up 0.4% to \$495 million from \$494 million in the prior-year quarter. Gross profit declined 4% to \$241 million from the prior-year quarter figure of \$250 million. Gross margin came in at 32.7% compared with the prior-year quarter figure of 33.7%.

Selling, general and administrative expenses declined 3% year over year to \$149 million from the prior-year quarter. Adjusted operating profit declined 5% year over year to \$91.6 million in the quarter. Operating margin came in at 12.4% compared with 13.0% in the year-ago quarter.

### Financial Update

Lincoln Electric had cash and cash equivalents of around \$200 million at the end of 2019 compared with \$359 million at the end of the 2018. The company reported record cash flow from operations of \$403 million during 2019 compared with \$329 million in the prior year.

During 2019, Lincoln Electric returned \$411 million to shareholders through dividend and share repurchases. The company's board of director's approved a new share repurchase program authorizing the company to repurchase up to 10 million of its outstanding common stock. This current authorization is in addition to the 2.8 million shares remaining from the prior program.

The board of directors recently declared an increase of 4.3% in the quarterly dividend to 49 cents per share. The dividend will be paid out on Jan 15, 2020 to shareholders of record as of Dec 31, 2019.

### 2019 Results

Lincoln Electric reported adjusted earnings per share of \$4.70 in 2019, down 2% from the prior year. The bottom line beat the Zacks Consensus Estimate of \$4.68. On a reported basis, including one-time items, earnings per share came in at \$4.68 compared with \$4.37 in 2018.

Sales dipped 0.8% year over year to \$3,003 million in 2019. The top-line figure also missed the Zacks Consensus Estimate of \$3,004 million.

### Outlook

The company is focusing on cost management to sustain margins in the backdrop of the weak of the broader deceleration in global industrial production. The initiatives include lower work hours, less overtime, suspending new hiring and cutting down discretionary spending. It is also implementing additional cost actions across the platform to achieve greater productivity. These actions are expected to contribute approximately \$15 million to \$18 million of annualized cost savings beginning in second-quarter 2020. Major portion of the benefits is expected to be realized in the back half of the year.

Given the deceleration in fourth quarter sales and the ongoing trend in January, the company expects top line and earnings growth to be impacted in the first half of the year. Lincoln Electric also anticipates headwinds from rising expected incentive compensation and projected higher tax rate in 2020 to impact earnings.

Quarter Ending **12/2019**

Report Date	Feb 13, 2020
Sales Surprise	-0.11%
EPS Surprise	1.77%
Quarterly EPS	1.15
Annual EPS (TTM)	4.69

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## Valuation

Lincoln Electric's shares are down 12.5% over the trailing 12-month period. Stocks in the Zacks Manufacturing – Tool & Related Products industry and the Zacks Industrial Products sector are down 20.9% and 19.7% over the past year, respectively.

The S&P 500 index has declined 5.0% in the past year.

The stock is currently trading at 15.87X forward 12-month earnings, which compares with 14.38X for the Zacks sub-industry, 16.24X for the Zacks sector and 17.7X for the S&P 500 index.

Over the past five years, the stock has traded as high as 25.36X and as low as 12.92X, with a 5-year median of 17.52X.

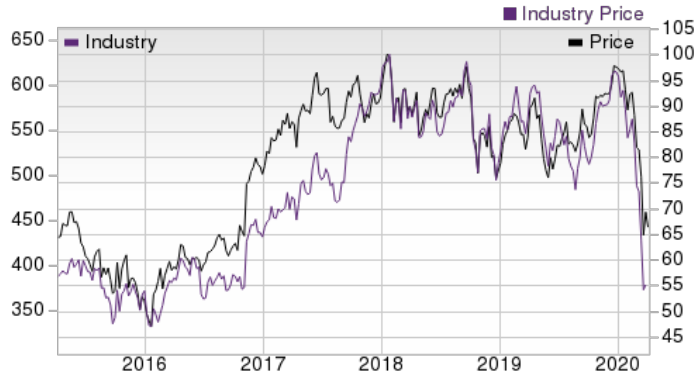
Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$82 price target reflects 16.74X Forward 12-month earnings.

The table below shows summary valuation data for LECO:

Valuation Multiples - LECO					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	15.87	14.39	16.24	17.7
	5-Year High	25.36	20.19	19.93	19.34
	5-Year Low	12.92	12.37	12.55	15.19
	5-Year Median	17.52	16.29	16.47	17.45
P/S F12M	Current	1.55	0.96	2.21	3.04
	5-Year High	2.6	1.52	2.72	3.44
	5-Year Low	1.34	0.84	1.52	2.54
	5-Year Median	1.81	1.17	1.99	3.01
EV/EBITDA TTM	Current	11.43	8.51	13.69	10.09
	5-Year High	23.58	13.01	17.37	12.87
	5-Year Low	8.17	6.26	10.71	8.27
	5-Year Median	13.69	9.89	14.75	10.78

As of 04/08/2020

## Industry Analysis Zacks Industry Rank: Bottom 6% (237 out of 253)



## Top Peers

Sandvik AB (SDVKY)	Outperform
Deere & Company (DE)	Neutral
John Bean Technologies Corporation (JBT)	Neutral
The Manitowoc Company, Inc. (MTW)	Neutral
Stanley Black & Decker, Inc. (SWK)	Neutral
Caterpillar Inc. (CAT)	Underperform
Kennametal Inc. (KMT)	Underperform
Terex Corporation (TEX)	Underperform

Industry Comparison Industry: Manufacturing - Tools & Related Products				Industry Peers		
	LECO Neutral	X Industry	S&P 500	CNHI Neutral	JBT Neutral	KMT Underperform
<b>VGM Score</b>	<b>C</b>	-	-	<b>B</b>	<b>D</b>	<b>C</b>
Market Cap	4.68 B	2.68 B	19.05 B	9.03 B	2.54 B	1.95 B
# of Analysts	7	6.5	13	6	5	6
Dividend Yield	2.52%	2.41%	2.23%	0.00%	0.50%	3.40%
<b>Value Score</b>	<b>D</b>	-	-	<b>A</b>	<b>C</b>	<b>B</b>
Cash/Price	0.05	0.14	0.06	0.77	0.02	0.07
EV/EBITDA	10.96	7.41	11.47	8.83	12.74	5.42
PEG Ratio	1.83	2.64	2.00	NA	3.78	4.74
Price/Book (P/B)	5.80	2.28	2.56	1.48	4.47	1.45
Price/Cash Flow (P/CF)	12.64	9.49	10.14	3.78	11.32	5.32
P/E (F1)	20.15	19.69	16.97	12.82	20.88	23.71
Price/Sales (P/S)	1.56	1.11	2.01	0.32	1.31	0.88
Earnings Yield	5.08%	5.08%	5.81%	7.77%	4.79%	4.21%
Debt/Equity	0.87	0.41	0.70	4.06	1.23	0.47
Cash Flow (\$/share)	6.15	3.14	7.01	1.77	7.10	4.42
<b>Growth Score</b>	<b>A</b>	-	-	<b>C</b>	<b>C</b>	<b>C</b>
Hist. EPS Growth (3-5 yrs)	8.62%	9.31%	10.92%	23.49%	28.51%	17.42%
Proj. EPS Growth (F1/F0)	-16.02%	-15.61%	-0.64%	-37.90%	-22.46%	-67.16%
Curr. Cash Flow Growth	-3.32%	4.61%	5.93%	-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	1.91	2.75	1.24	5.81	1.49	2.53
Debt/Capital	46.51%	27.44%	42.36%	80.26%	55.08%	31.85%
Net Margin	9.76%	7.48%	11.64%	5.06%	6.63%	5.89%
Return on Equity	35.24%	12.55%	16.74%	19.87%	30.75%	11.97%
Sales/Assets	1.27	0.80	0.54	0.60	1.07	0.85
Proj. Sales Growth (F1/F0)	-10.41%	-1.05%	0.61%	-14.04%	-9.19%	-13.97%
<b>Momentum Score</b>	<b>F</b>	-	-	<b>F</b>	<b>F</b>	<b>F</b>
Daily Price Chg	6.85%	4.16%	4.33%	6.36%	5.20%	5.47%
1 Week Price Chg	-4.26%	-0.56%	-4.40%	-6.60%	-12.83%	4.28%
4 Week Price Chg	8.09%	-6.38%	-1.70%	-10.68%	7.54%	16.79%
12 Week Price Chg	-18.91%	-25.90%	-20.64%	-37.94%	-27.48%	-34.37%
52 Week Price Chg	-12.45%	-20.48%	-12.97%	-37.65%	-18.51%	-40.77%
20 Day Average Volume	600,410	98,699	4,016,075	2,150,504	294,410	1,518,132
(F1) EPS Est 1 week change	-1.78%	-1.78%	-0.26%	0.00%	-7.68%	-6.30%
(F1) EPS Est 4 week change	-16.20%	-16.20%	-5.64%	-33.69%	-26.07%	-24.49%
(F1) EPS Est 12 week change	-22.39%	-22.39%	-7.49%	-39.94%	-26.24%	-44.29%
(Q1) EPS Est Mthly Chg	-29.12%	-32.42%	-9.90%	-44.13%	-34.58%	-47.57%

## 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>D</b>
Growth Score	<b>A</b>
Momentum Score	<b>F</b>
VGM Score	<b>C</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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