

3M Company (MMM)

\$156.59 (As of 02/03/20)

Price Target (6-12 Months): **\$164.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 07/05/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: C

Growth: B

Momentum: F

Summary

3M stands to gain from its solid product portfolio, restructuring actions and shareholder-friendly policies over the long run. Also, the company's acquisitions and divestments will work in its favour. It recently communicated that it intends to transform its businesses through streamlined operational structure and new operating model (global). Its recent restructuring moves are anticipated to yield pre-tax savings of \$40-50 million in 2020. In fourth-quarter 2019, the company's earnings and sales lagged estimates by 7.1% and 0.2%, respectively. For 2020, 3M anticipates earnings of \$9.30-\$9.75 per share and sales to increase 3-5% year over year. High tax rates, forex woes and 2019-headwinds are predicted to adversely impact earnings. Over the past three months, the company's shares have underperformed the industry.

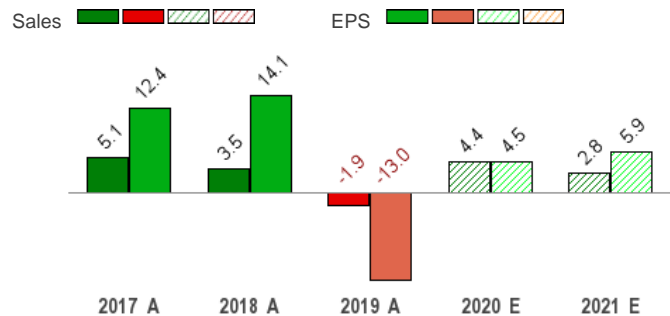
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$219.75 - \$150.58
20 Day Average Volume (sh)	3,327,499
Market Cap	\$90.0 B
YTD Price Change	-11.2%
Beta	1.13
Dividend / Div Yld	\$5.76 / 3.7%
Industry	Diversified Operations
Zacks Industry Rank	Bottom 25% (190 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-7.1%
Last Sales Surprise	-0.2%
EPS F1 Est- 4 week change	-1.4%
Expected Report Date	04/23/2020
Earnings ESP	0.0%
P/E TTM	17.5
P/E F1	16.5
PEG F1	1.6
P/S TTM	2.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	8,298 E	8,691 E	8,559 E	8,447 E	34,513 E
2020	8,230 E	8,528 E	8,447 E	8,282 E	33,564 E
2019	7,863 A	8,171 A	7,991 A	8,111 A	32,136 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.30 E	\$2.59 E	\$2.61 E	\$2.55 E	\$10.07 E
2020	\$2.15 E	\$2.40 E	\$2.56 E	\$2.39 E	\$9.51 E
2019	\$2.23 A	\$2.20 A	\$2.58 A	\$1.95 A	\$9.10 A

*Quarterly figures may not add up to annual.

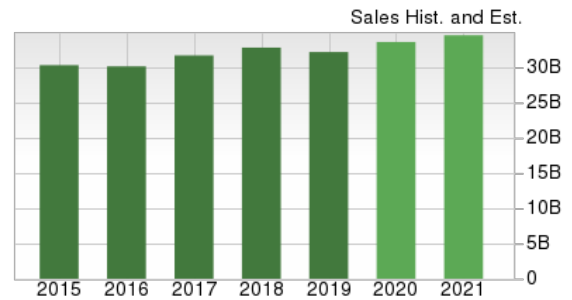
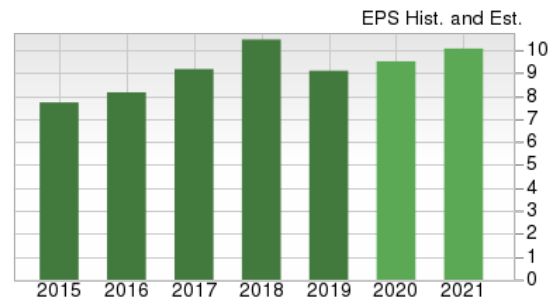
The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 02/03/2020. The reports text is as of 02/04/2020.

Overview

Headquartered in St. Paul, MN, and founded in 1902, 3M Company together with its subsidiaries operates as a diversified technology firm. It has manufacturing operations across the globe and serves diversified customer base primarily in the United States, Europe, Middle East and Africa; Latin America/Canada; and the Asia Pacific regions. Exiting 2018, the company had 96,000 employees.

Effective from the second quarter of 2019, the company realigned its business segments from five to four — including Safety & Industrial; Transportation & Electronics; Health Care; and Consumer. The segmental information is briefly discussed below.

- The **Safety & Industrial** segment mainly serves customers in the electrical, safety and industrial markets across the globe. The segment includes adhesives and tapes, personal safety, abrasives, closure and masking systems, roofing granules, automotive aftermarket, electrical and communication markets, and other related businesses.
- The **Transportation & Electronics** segment primarily serves original equipment manufacturers (OEMs) in the electronics and transportation industries across the globe. The segment includes electronics, commercial solutions, advanced materials, transportation safety, automotive and aerospace, and other related businesses.
- The **Health Care** segment engages in serving customers in the global healthcare industry. Businesses within the segment are oral care, drug delivery, medical solutions, food safety, separation and purification sciences, health information systems, and other miscellaneous healthcare businesses.
- The **Consumer** segment provides office supply products, stationery products, home improvement products, home care products and consumer health care products. In addition, the segment's Construction and Home Improvement Division offers some retail auto care products.



Reasons To Buy:

- ▲ In the quarters ahead, 3M intends to become more competent on the back of product-portfolio solidification. The company's household products like Nexcare, Post-it, Scotch, Scotch-Brite and Scotchgard are market leaders in their individual categories. Also, 3M's value model that comprises four priorities, namely Portfolio (detailed in the next point), Innovation, Transformation, and People and Culture helps strengthening its margins. In addition, the company recently communicated that it intends to transform its businesses through a streamlined operational structure and its new operating model (global).
- ▲ In sync with its Portfolio priority, 3M completed the divestiture of the communication markets business in 2018, gas and flame detection business to Teledyne Technologies in August 2019 and advanced ballistic-protection business to Avon Rubber in January 2020. Also, the company signed an agreement to divest its drug delivery business to an affiliate of Altaris Capital Partners. This divestment is anticipated to be complete in the first half of 2020. Further, 3M acquired the technology business of M*Modal, a prominent healthcare technology provider of conversational Artificial Intelligence-powered systems, in February 2019. The buyout has been strengthening the company's health information systems business and will likely continue aiding it over the long term. Moreover, it completed the acquisition of Acelytic Inc and its KCI subsidiaries in October 2019. The buyout will fortify 3M's medical solutions business under the Health Care segment. Notably, its acquired assets and divestments had a net positive impact of 5.1% on sales in the fourth quarter. The company envisions a 3% positive impact from acquisitions (net of impact from divested assets) in 2020.
- ▲ 3M worked on restructuring and other actions to cut costs, boost productivity and increase cash flow generation (by lowering capital investments, reducing inventories and increasing indirect cost actions) in the second quarter of 2019. 3M predicts annual pre-tax savings of \$225-\$250 million from these actions. Also, concurrent with the fourth-quarter results, the company announced that it undertook restructuring moves that are likely to lower workforce by 1,500. Pre-tax savings from the restructuring measures are anticipated to be \$110-\$120 million with \$40-50 million expected in 2020.
- ▲ The company remains committed to rewarding its shareholders handsomely through dividend payments and share buybacks. In 2019, it paid out dividends totaling \$3,316 million to its shareholders and bought back shares worth \$1,407 million. It is worth mentioning here that the company hiked the quarterly dividend rate by 6% in February 2019. Also, a share buyback program worth \$10 billion was approved in November 2018. For 2020, the company anticipates buying back shares worth \$1 billion.

3M expects to gain from a solid product portfolio, restructuring actions, acquired assets and shareholder-friendly policies.

Reasons To Sell:

- ▼ Over the past three months, 3M's shares have decreased 10.7% versus the industry's growth of 2.5%. In the fourth quarter, the company's earnings and sales missed estimates by 7.1% and 0.2%, respectively. In the quarter, organic sales dipped 2.6% year over year, mainly due to softness in automotive and electronics businesses. Also, sales in the Asia Pacific slid 1.7% and that in Europe, the Middle East and Africa (EMEA) slipped 2% year over year. Along with weak organic sales, the Acelity buyout and organizational realignment charges adversely impacted earnings. For 2020, the company predicts year-over-year change in Transportation and Electronics' organic sales to be (2%)-2%, while the same for the Asia Pacific region will likely be (1%)-1% and for EMEA region will be within (1%)-3%. These seem to have created bearish sentiments for the stock. In the past seven days, the company's earnings estimates have been lowered 0.9% to \$9.51 for 2020 and 1.5% to \$10.07 for 2021.
- ▼ Rising cost of sales was the major cause for concern regarding 3M over the last few quarters. The company's cost of sales increased 6.5% year over year in the fourth quarter of 2019. Also, in the fourth quarter, selling, general and administrative expenses grew 15.3% while research, development and related expenses expanded 19.2%. We believe that the rising costs, if not checked, might continue to weigh on the company's profitability in the quarters ahead. For 2020, the company expects adverse impacts of 25 cents on its earnings from 2019-headwinds. Also, the impact of higher tax rate will leave a negative effect of 10 cents to flat on earnings.
- ▼ Geographical diversification is reflective of 3M's flourishing business. However, the diversity exposed the company to headwinds arising from geopolitical issues, macroeconomic challenges and unfavorable movements in foreign currencies. In the fourth quarter, forex woes had an adverse 0.4% impact on sales. For 2020, the company predicts an adverse impact of 5 cents on earnings per share. Further, the company faces tremendous local competitive pressure whether it is in Brazil, China, India or Indonesia. In order to reduce the competitive pressure, it has to invest significantly in R&D to locally develop and manufacture products. These are likely to put pressure on its finances and hence might impact profitability.
- ▼ A highly leveraged balance sheet can inflate 3M's financial obligations and subsequently hurt profitability. In the last five years (2015-2019), the company's long-term debt rose 14.9% (CAGR). Notably, the metric stood at \$17.5 billion at the end of the fourth quarter of 2019, up 30.6% above the 2018-level. Interest expense (after tax) surged 34% year over year to \$0.36 billion in 2019. Also, the company seems to be more leveraged than the industry with the respective long-term debt-to-capital ratios of 63.4% and 56.6%. For 2020, the company expects interest expense (after tax) to be approximately \$0.4 billion.

Weakness in electronics and softness in the Asia Pacific and EMEA markets are expected to impact organic sales in 2020. High tax rates, huge debts and forex woes are concerning too.

Last Earnings Report

3M Q4 Earnings Fall Short of Estimates, Decline Y/Y

3M Company has reported weaker-than-expected results for the fourth quarter of 2019, with earnings and sales lagging estimates by 7.1% and 0.2%, respectively.

Its adjusted earnings in the reported quarter were \$1.95 per share. The figure lagged the Zacks Consensus Estimate of \$2.10. Also, its bottom line declined 15.6% from the year-ago quarter figure of \$2.31 due to organic sales decline, the Acelity buyout and organizational realignment charges.

For 2019, the company's adjusted earnings were \$9.10 per share, decreasing 13% year over year. However, the bottom line surpassed the Zacks Consensus Estimate of \$9.04.

Quarter Ending **12/2019**

Report Date	Jan 28, 2020
Sales Surprise	-0.19%
EPS Surprise	-7.14%
Quarterly EPS	1.95
Annual EPS (TTM)	8.96

Weak Organic Sales, Divestitures and Forex Woes Hurt Revenues

In the quarter under review, 3M's net sales were \$8,111 million, reflecting growth of 2.1% from the year-ago quarter. Results were adversely impacted by a 2.6% decrease in organic sales (results in automotive and electronics businesses were soft in the quarter), 0.5% negative impact of divestitures and 0.4% adverse impact of foreign currency translation, partially offset by 5.6% gain from acquisitions.

However, the company's net sales lagged the Zacks Consensus Estimate of \$8,126 million.

On a geographical basis, sales in the United States grew 7.4% year over year, while that in the Asia Pacific declined 1.7%. Europe, Middle East and Africa's sales declined 2% and that of Latin America/Canada improved 1.2%.

Effective from the second quarter of 2019, the company realigned its business segments from five to four — including Safety & Industrial; Transportation & Electronics; Health Care; and Consumer. The segmental information is briefly discussed below.

Revenues from the **Safety and Industrial** segment totaled \$2,811 million, declining 4.8% year over year. The decline resulted from a 0.6% adverse impact of forex woes, 2.8% fall in organic sales and 1.4% negative impact of divestitures.

Revenues from the **Transportation & Electronics** segment totaled \$2,290 million, declining 6.2% year over year. Results were adversely impacted by a 5.9% fall in organic sales and a 0.3% decline from forex woes.

Revenues from the **Health Care** segment were \$2,141 million, rising 25.4% year over year. Acquisitions had positive impacts of 26%, while organic sales declined 0.2% and forex woes had adverse impacts of 0.4%.

Revenues from the **Consumer** segment were flat year over year at \$1,268 million. Forex woes had an adverse impact of 0.2%, offset by 0.2% increase in organic sales.

In 2019, the company's net sales were \$32,136 million, reflecting a 1.9% decline from the previous year. However, the top line met with the Zacks Consensus Estimate of \$32.13 billion.

Operating Margin Down Y/Y

In the quarter under review, 3M's cost of sales rose 6.5% year over year to \$4,325 million. It represented 53.3% of net sales compared with 51.1% in the year-ago quarter. Selling, general and administrative expenses increased 15.3% year over year to \$1,940 million. It represented 23.9% of net sales versus 21.2% in the year-ago quarter. Research, development and related expenses grew 19.2% to \$521 million. It represented 6.4% of the quarter's net sales versus 5.5% in the year-ago quarter.

Adjusted operating income in the quarter under review declined 13.7% year over year to \$1,539 million. Operating margin decreased 340 bps year over year to 19% due mainly to adverse impacts of the Acelity buyout, global organizational restructuring actions, lower organic volumes and others. Tax rate in the quarter was 20.3% versus 20.5% in the year-ago quarter.

Balance Sheet and Cash Flow

Exiting the fourth quarter, 3M had cash and cash equivalents of \$2,353 million, down 70% from \$7,731 million at the end of the last reported quarter. Long-term debt balance was roughly flat sequentially at \$17,518 million.

In the reported quarter, the company generated net cash of \$2,338 million, reflecting year-over-year growth of 3.5%. Capital used for purchasing property, plant and equipment grew 1.3% year over year to \$538 million. Free cash flow in the quarter was \$1,800 million versus \$1,727 generated in the year-ago quarter. Free cash flow conversion was at 186%.

During 2019, the company used \$3,316 million for paying out dividends to shareholders, while repurchased \$1,407 million shares.

Outlook

3M intends on transforming its businesses through streamlined operational structure and new operating model (global). For these changes, the company has undertaken restructuring actions (that are likely to lower workforce by 1,500). Pre-tax savings from the restructuring measures are anticipated to be \$110-\$120 million, with \$40-50 million expected in 2020.

For 2020, the company anticipates earnings of \$9.30-\$9.75 per share. Tax rate is likely to be 20-21%.

Sales are predicted to increase 3-5% year over year. Organic sales will likely be between flat and 2% rise. Acquisitions, net of impact from divested assets, will likely have 3% positive impact. Forex woes will have neutral impact.

Net cash generated from operating activities is anticipated to be \$6.9-\$7.6 billion, while capital expenditure will likely total \$1.6-\$1.8 billion. Free cash flow is predicted to be \$5.1-\$6 billion, while free cash flow conversion will likely be 95-105%.

Further, shares worth \$1 billion will likely be repurchased during 2020. Return on invested capital will likely be 18-21%.

Recent News

Divestiture of Ballistic Protection Business

On **Jan 2, 2020**, 3M announced that it completed the divestiture of its advanced-ballistic protection business in a \$91-million transaction. The other party to the transaction was Avon Rubber p.l.c.

3M's advanced-ballistic protection business (with annual sales of \$85 million) formerly was under the Advanced Materials Division, which is part of the company's Transportation & Electronics segment.

As part of the transaction, 3M sold its flat armor, body armor, ballistic helmets and various helmet-attachment products. These products are mainly used by law enforcement and government customers. Also, advanced-ballistic protection business' 280 employees will now work for Avon Rubber.

The transaction will enable 3M to concentrate on more relevant businesses. Earnings impact of the advanced-ballistic protection business divestiture will be neutral.

Divestment of Drug Delivery Business to Altaris Capital Unit

On **Dec 12, 2019**, 3M announced that it has inked an agreement with an affiliate of Altaris Capital Partners, LLC to divest considerably all of its drug delivery business. The deal, worth of about \$650 million, includes cash, a 17% noncontrolling interest in the new company and an interest-bearing security. The deal is subject to customary closing conditions and regulatory approvals, and is projected to close in the first half of 2020.

3M's drug delivery business is engaged in developing and producing pharmaceutical products, leveraging transdermal, inhalation and conventional drug delivery technologies. It's worth noting here that the business considered for divestment has annual global sales of roughly \$380 million. Meanwhile, the company will continue to operate its transdermal drug delivery components business.

As noted by 3M, about 900 employees of its drug delivery business are likely to join the new company as a result of the divestment. As a matter of fact, the deal will enable the company to emphasize on its core health care business.

On completion, the deal is likely to lead to a gain of 45 cents to 50 cents per share for 3M. The company will report its ownership interest in the drug delivery business with the help of the equity method of accounting.

Dividend

On **Dec 12, 2019**, 3M paid a quarterly cash dividend of \$1.44 per share to shareholders of record as on Nov 22, 2019.

Establishment Of New Committee

On **Nov 25, 2019**, 3M announced the establishment of a new committee for providing oversight of its strategies linked to commercialization, research and development, sustainability, environmental stewardship as well as other related activities.

Valuation

3M's shares have moved down 11.2% in the year-to-date period and 22.1% over the trailing 12 months. Stocks in both the Zacks sub-industry and the Zacks Conglomerates sector made no change in the year-to-date period. Over the past year, both the Zacks sub-industry and sector have increased 13.6%.

The S&P 500 index has moved up 0.9% year to date and 17.8% in the past year.

The stock is currently trading at 12.6x forward 12-month EBITDA, which compares to 26.85x for the Zacks sub-industry, 26.85x for the Zacks sector and 12.66x for the S&P 500 index.

Over the past five years, the stock has traded as high as 16.37x and as low as 10.18x, with a 5-year median of 12.61x. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$164 price target reflects 17.19x forward 12-month earnings per share.

The table below shows summary valuation data for MMM.

Valuation Multiples - MMM					
		Stock	Sub-Industry	Sector	S&P 500
	Current	12.6	26.85	26.85	12.66
5-YEAR HIGH	16.37	24.18	24.18	24.18	18.88
5-YEAR LOW	10.18	10.18	10.18	10.18	10.18
5-YEAR MEDIAN	12.61	12.61	12.61	12.61	12.61

EV/EBITDA F12M	5-Year High	16.37	81.18	81.18	12.66
	5-Year Low	10.18	17.86	17.86	9.08
	5-Year Median	12.61	22.15	22.15	10.78
P/E F12M	Current	16.37	19.57	19.57	18.61
	5-Year High	26.25	20.06	20.06	19.34
	5-Year Low	15.31	15.31	15.31	15.18
	5-Year Median	19.34	17.76	17.76	17.46
EV/Sales F12M	Current	3.25	4.22	4.22	3.26
	5-Year High	4.87	4.24	4.24	3.37
	5-Year Low	2.89	2.84	2.84	2.3
	5-Year Median	3.73	3.65	3.65	2.78

As of 02/03/2020

Industry Analysis Zacks Industry Rank: Bottom 25% (190 out of 254)



Top Peers

Avery Dennison Corporation (AVY)	Neutral
Carlisle Companies Incorporated (CSL)	Neutral
Danaher Corporation (DHR)	Neutral
Federal Signal Corporation (FSS)	Neutral
Honeywell International Inc. (HON)	Neutral
IDEX Corporation (IEX)	Neutral
Parker-Hannifin Corporation (PH)	Neutral
United Technologies Corporation (UTX)	Underperform

Industry Comparison Industry: Diversified Operations				Industry Peers		
	MMM Neutral	X Industry	S&P 500	AVY Neutral	CSL Neutral	HON Neutral
VGM Score	C	-	-	B	A	B
Market Cap	90.05 B	7.31 B	23.66 B	11.19 B	8.96 B	122.41 B
# of Analysts	7	2.5	13	6	3	10
Dividend Yield	3.68%	1.44%	1.82%	1.73%	1.26%	2.10%
Value Score	C	-	-	C	C	C
Cash/Price	0.03	0.14	0.04	0.02	0.07	0.08
EV/EBITDA	12.38	9.08	13.87	24.65	14.34	13.67
PEG Ratio	1.63	2.10	1.97	2.38	1.18	2.10
Price/Book (P/B)	8.89	1.33	3.24	9.29	3.34	6.54
Price/Cash Flow (P/CF)	12.74	11.61	13.40	15.12	16.52	17.37
P/E (F1)	16.62	17.06	18.48	19.02	17.67	19.43
Price/Sales (P/S)	2.80	1.45	2.60	1.58	1.89	3.33
Earnings Yield	6.07%	5.66%	5.40%	5.25%	5.66%	5.14%
Debt/Equity	1.73	0.75	0.72	1.25	0.59	0.59
Cash Flow (\$/share)	12.30	1.94	6.92	8.86	9.57	9.86
Growth Score	B	-	-	A	A	B
Hist. EPS Growth (3-5 yrs)	5.88%	9.90%	10.80%	17.83%	11.65%	8.56%
Proj. EPS Growth (F1/F0)	4.52%	5.71%	7.46%	6.72%	11.87%	8.03%
Curr. Cash Flow Growth	-9.16%	2.93%	10.59%	3.06%	9.03%	-1.43%
Hist. Cash Flow Growth (3-5 yrs)	2.13%	4.88%	8.55%	8.17%	11.06%	5.69%
Current Ratio	1.41	2.05	1.21	1.04	3.04	1.34
Debt/Capital	63.37%	41.54%	42.91%	55.46%	37.23%	37.28%
Net Margin	14.22%	5.35%	11.76%	4.29%	9.66%	16.73%
Return on Equity	51.39%	10.40%	17.24%	51.98%	17.99%	32.21%
Sales/Assets	0.78	0.77	0.55	1.31	0.88	0.62
Proj. Sales Growth (F1/F0)	4.44%	2.84%	4.22%	3.79%	5.15%	2.75%
Momentum Score	F	-	-	F	C	A
Daily Price Chg	-1.30%	0.00%	0.67%	2.09%	1.21%	-1.10%
1 Week Price Chg	-10.94%	-1.99%	-2.60%	1.20%	-0.19%	-2.21%
4 Week Price Chg	-12.33%	-2.43%	-0.76%	5.59%	-1.99%	-3.49%
12 Week Price Chg	-7.95%	-2.54%	2.84%	0.39%	-0.33%	-5.26%
52 Week Price Chg	-21.79%	-7.96%	13.93%	29.24%	43.47%	15.81%
20 Day Average Volume	3,327,499	48,821	1,915,782	528,654	363,739	2,455,868
(F1) EPS Est 1 week change	-0.97%	0.00%	0.00%	-0.14%	0.00%	0.17%
(F1) EPS Est 4 week change	-1.38%	0.00%	0.00%	-0.14%	-0.55%	0.07%
(F1) EPS Est 12 week change	-1.54%	-1.09%	-0.13%	-0.24%	-1.09%	0.07%
(Q1) EPS Est Mthly Chg	-3.55%	-4.09%	0.00%	-3.42%	-4.64%	-0.29%

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	F
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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