

Meritor, Inc.(MTOR)
\$23.55 (As of 08/06/20)

Price Target (6-12 Months): **\$25.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 07/24/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: B

Growth: F

Momentum: D

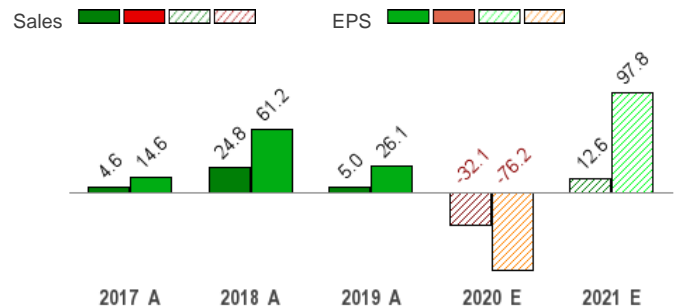
Summary

Meritor's regularly introduces products that position it as a market leader in electric drivetrains and has enabled it to clinch contracts from MAN, Mercedes Benz and Iveco. The company's buyout of AxleTech has enhanced its exposure in adjacent end markets served, which will support its target of realizing more than \$15 million in annual cost synergies by fiscal 2022. It is likely to gain from higher margins tied to OEM adoption of advanced products. However, depressed demand of vehicles and weak consumer sentiment amid the COVID-19 will mar its near-term revenues and earnings. In fact, for fourth-quarter fiscal 2020, Meritor projects sales in the band of around \$700 million, implying a year over year decline of 32%. High debt of the firm also plays a spoilsport. As such, the investors are recommended to wait for a better entry point.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	\$27.18 - \$10.91
20 Day Average Volume (sh)	703,316
Market Cap	\$1.7 B
YTD Price Change	-10.1%
Beta	2.46
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Automotive - Original Equipment
Zacks Industry Rank	Top 48% (121 out of 252)

Sales and EPS Growth Rates (Y/Y %)


Last EPS Surprise	31.9%
Last Sales Surprise	12.7%
EPS F1 Est- 4 week change	1.5%
Expected Report Date	11/11/2020
Earnings ESP	0.0%
P/E TTM	13.5
P/E F1	25.9
PEG F1	NA
P/S TTM	0.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					3,356 E
2020	901 A	871 A	514 A	694 E	2,980 E
2019	1,038 A	1,156 A	1,166 A	1,028 A	4,388 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$1.80 E
2020	\$0.64 A	\$0.74 A	-\$0.47 A	-\$0.08 E	\$0.91 E
2019	\$0.79 A	\$1.03 A	\$1.20 A	\$0.83 A	\$3.82 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 08/06/2020. The reports text is as of 08/07/2020.

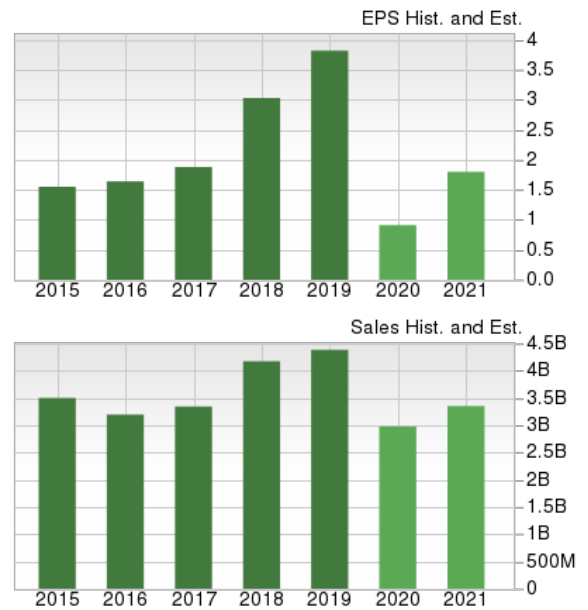
Overview

Meritor, Inc. headquartered in Troy, MI, is a global automotive parts manufacturer and supplier. The company supplies a broad range of integrated systems, modules and components for commercial and specialty vehicles worldwide, with leading positions in most of its markets. Meritor serves a broad range of original equipment manufacturers (OEMs) worldwide, including commercial truck, trailer, military, bus and coach, other industrial OEMs and certain aftermarkets.

From Mar 12, 2018, the company changed its reportable segments. The two new segments are:

Commercial Truck & Trailer (79.6% of revenues in fiscal 2019): The segment supplies drivetrain systems and components, including axles, drivelines, and braking and suspension systems, primarily for medium- and heavy-duty trucks in North America, South America and the Asia Pacific. It also offers a varied range of undercarriage products and systems for trailer applications in North America. This segment also includes the company's aftermarket businesses in the Asia Pacific and South America.

Aftermarket & Industrial (24.5%): This segment supplies axle, brakes, drivelines, suspension parts and other replacement parts to commercial vehicle and industrial aftermarket customers, primarily in North America and Europe. The segment also supplies a wide variety of drivetrain system and certain components, including axles, drivelines, brakes and suspension systems for in North America.



Note: The percentage share of segment revenues in total revenues includes inter-segment sales.



Reasons To Buy:

- ▲ While Meritor has successfully executed the three-year M2019 program, it is on track to achieve M2022 goals that focus on new business opportunities, margin expansion and cost-containment efforts. Per the M2022 goals, the firm is expected to achieve the margin target of 12.5% and remain committed to return money to its shareholders. The company's improving free cash flow and investor friendly moves bode well.
- ▲ Meritor's buyout of AxleTech has enhanced its growth. The buyout led to the introduction of a complementary product portfolio, providing the company with a full line of independent suspensions, material handling axles, new braking solutions and drivetrain components. It also diversified Meritor's exposure in adjacent end markets served, which will support its target of realizing more than \$15 million in annual cost synergies by fiscal 2022.
- ▲ The company regularly introduces products that position it as a market leader in electric drivetrains. These product introductions have enabled it to clinch contracts from MAN, Mercedes Benz and Iveco. The expanding product portfolio will enable the company to meet the changing needs of customers. In addition, it announced 22 electrification programs with global OEMs that are expected to put nearly 130 fully-electric medium and heavy-duty commercial trucks on road through 2020. The company is likely to gain from higher margins tied to OEM adoption of advanced products such as eAxle, air disc brakes and precision gearing.
- ▲ In response to the uncertainty caused by the coronavirus pandemic, Meritor has initiated a series of cost savings across the company including substantial staffing adjustments, and compensation cuts. These restructuring actions represent a reduction of 8% in global wage positions. Meritor anticipates that this turnaround program would help in achieving more than \$30 million of run rate savings through the M2022 time frame. The focus on cost discipline may provide the firm some respite amid the financial crisis.

Meritor's buyout of AxleTech has enhanced its growth prospects and is likely to result into various synergies.

Reasons To Sell:

- ▼ The coronavirus pandemic has crippled the auto industry, and will lead to decline in sales and production, hurting the automotive parts manufacturer and supplier. Meritor suspended its share buyback program in response to disruptions to the company's supply chain due to the pandemic-led crisis. Weak consumer sentiment amid the pandemic is likely to hurt its sales and earnings of Meritor in the near future.
- ▼ For fourth-quarter fiscal 2020, Meritor projects sales of \$700 million approximately, implying a year over year decline of 32%. Cash flow from operations and free cash flow are anticipated to be around \$65 million and \$25 million, respectively, down from \$143 million and \$124 million in the year-ago period. Further, the firm anticipates adjusted net loss from continuing operations of approximately 10 cents per share in Q4, down from EPS of 83 cents recorded in the prior-year quarter.
- ▼ Meritor's high debt is a spoilsport. Long-term debt was \$1,193 million at the end of the fiscal third quarter, marking a rise from \$902 million as of Sep 30, 2019. Its total debt to capital stands at 0.75 versus the industry's 0.45, restricting its financial freedom to tap onto growth opportunities.
- ▼ Trade tensions and slowdown in global economic growth are playing spoilsports for truck makers. Amid sluggish freight volumes, truck makers are logging lower orders. Due to macroeconomic headwinds, the truck manufactures are not expecting market conditions and sales to improve in the near term as well. Softening heavy-duty truck markets in the United States and declining demand for Class 8 trucks are likely to weigh on commercial truck and industrial parts makers like Meritor.

For the fourth-quarter fiscal 2020, Meritor projects sales of about \$700 million, implying a year over year decline of 32%.

Last Earnings Report

Meritor Q3 Earnings Loss Narrower-Than-Expected

Meritor posted an adjusted loss of 47 cents per share in third-quarter fiscal 2020 (ended Jun 30, 2020), narrower than the Zacks Consensus Estimate of loss of 69 cents. Higher-than-anticipated revenues from the Commercial Truck & Trailer segment resulted in this narrower-than-estimated loss. Revenues from the segment came in at \$336 million, beating the consensus mark of \$222 million.

The bottom line declined from the year-ago adjusted earnings of \$1.20 a share. Adjusted loss from continuing operations was \$34 million as against the adjusted income of \$103 million recorded in third-quarter fiscal 2019.

Sales plummeted 56% year over year to \$514 million in the fiscal third quarter. This year-over-year decline was due to lower market volumes resulting from weak customer demand and government mandates amid the coronavirus pandemic. However, the reported figure surpassed the Zacks Consensus Estimate of \$456 million in the quarter.

Adjusted EBITDA tanked to \$7 million from the year-earlier quarter's \$146 million. Adjusted EBITDA margin was 1.4% compared with the prior year's 12.5%.

Segment Results

Revenues in the Commercial Truck & Trailer segment amounted to \$336 million in the fiscal third quarter, slumping 64% year over year on lower market volumes, resulting from decreased customer demand and government mandates amid the pandemic. However, the figure outpaced the Zacks Consensus Estimate of \$222 million. The segment reported negative adjusted EBITDA of \$23 million as against the positive EBITDA of \$97 million witnessed in the year-ago quarter. EBITDA margin declined to negative 6.8% during the quarter from the positive 10.5% recorded in the prior-year quarter.

Revenues in the Aftermarket & Industrial segment totaled \$203 million, down 28% from the year-ago level, primarily on dismal production volumes across most markets served, partly offset by revenues generated from the AxleTech acquisition. The revenue figure also missed the Zacks Consensus Estimate of \$222 million. The segment's adjusted EBITDA was \$31 million compared with the year-ago quarter's \$50 million. EBITDA margin declined to 15.3% from the prior-year period's 17.7%.

Financial Position

In the reported quarter, Meritor's cash and cash equivalents summed \$280 million as of Jun 30, 2020, compared with \$108 million as of Sep 30, 2019. Long-term debt was \$1,193 million at the end of the fiscal third quarter, marking a rise from \$902 million as of Sep 30, 2019.

Meritor's cash outflow from operating activities as of Jun 30, 2020, was \$102 million, as against the inflow of \$143 million witnessed in the year-ago quarter. For the quarter ended Jun 30, 2020, capital expenditure was \$12 million compared with the year-ago quarter's \$19 million.

Outlook

For fourth-quarter fiscal 2020, Meritor projects sales of \$700 million approximately. Cash flow from operations and free cash flow are anticipated to be around \$65 million and \$25 million, respectively. Further, the firm anticipates adjusted net loss from continuing operations of approximately 10 cents.

Quarter Ending 06/2020

Report Date	Jul 29, 2020
Sales Surprise	12.70%
EPS Surprise	31.88%
Quarterly EPS	-0.47
Annual EPS (TTM)	1.74

Valuation

Meritor's shares are down 10.1% in the year-to-date period and up 17.9% over the trailing 12-month period. Stocks in the Zacks Automotive - Original Equipment industry and the Zacks Automotive sector are down 6.1% and up 20%, respectively, in the year-to-date period. Over the past year, the Zacks sub-industry and sector are up 1.5% and 36.7%, respectively.

The S&P 500 index is up 3.2% in the year to date period and up 13.5% in the past year.

The stock is currently trading at 17.23X forward 12-month earnings, which compares to 23.08X for the Zacks sub-industry, 24.39X for the Zacks sector and 22.69X for the S&P 500 index.

Over the past five years, the stock has traded as high as 17.68X and as low as 3.66X, with a 5-year median of 7.13X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$25 price target reflects 18.25X forward 12-month earnings per share.

The table below shows summary valuation data for MTOR:

Valuation Multiples - MTOR					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	17.23	23.08	24.39	22.69
	5-Year High	17.68	25.87	25.33	22.69
	5-Year Low	3.66	8.36	8.2	15.25
	5-Year Median	7.13	11.41	9.87	17.55
EV/EBITDA TTM	Current	8.18	5.75	11.65	12.89
	5-Year High	24.77	8.44	11.75	12.89
	5-Year Low	NA	3.94	6.8	8.24
	5-Year Median	5.49	6.32	9.28	10.89
P/S F12M	Current	0.52	0.68	0.88	3.63
	5-Year High	0.73	0.78	0.88	3.63
	5-Year Low	0.16	0.44	0.49	2.53
	5-Year Median	0.42	0.61	0.61	3.04

As of 08/06/2020

Industry Analysis Zacks Industry Rank: Top 48% (121 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Garrett Motion Inc. (GTX)	Outperform	1
Strattec Security Corporation (STRT)	Outperform	2
Dana Incorporated (DAN)	Neutral	3
Gentex Corporation (GNTX)	Neutral	3
Lear Corporation (LEA)	Neutral	3
Magna International Inc. (MGA)	Neutral	2
Oshkosh Corporation (OSK)	Neutral	3
Veoneer, Inc. (VNE)	Neutral	3

Industry Comparison Industry: Automotive - Original Equipment				Industry Peers		
	MTOR	X Industry	S&P 500	DAN	OSK	VNE
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	D	-	-	C	C	D
Market Cap	1.70 B	959.93 M	23.20 B	1.80 B	5.45 B	1.14 B
# of Analysts	2	2	14	5	10	1
Dividend Yield	0.00%	0.00%	1.78%	0.00%	1.50%	0.00%
Value Score	B	-	-	A	B	F
Cash/Price	0.17	0.19	0.07	0.43	0.06	0.76
EV/EBITDA	5.02	5.64	13.21	6.30	6.45	-1.24
PEG Ratio	NA	2.24	2.94	89.47	1.95	NA
Price/Book (P/B)	4.22	1.39	3.12	1.05	1.97	0.80
Price/Cash Flow (P/CF)	4.66	4.91	12.27	2.26	7.80	NA
P/E (F1)	25.92	28.86	21.69	90.36	17.29	NA
Price/Sales (P/S)	0.51	0.46	2.48	0.25	0.75	0.78
Earnings Yield	3.86%	1.73%	4.39%	1.12%	5.79%	-43.38%
Debt/Equity	2.96	0.56	0.77	1.72	0.30	0.14
Cash Flow (\$/share)	5.05	2.94	6.94	5.52	10.26	-3.46
Growth Score	F	-	-	C	F	C
Hist. EPS Growth (3-5 yrs)	22.00%	8.02%	10.46%	9.78%	29.37%	NA
Proj. EPS Growth (F1/F0)	-76.18%	-54.67%	-6.80%	-95.49%	-44.33%	10.16%
Curr. Cash Flow Growth	15.83%	-4.87%	5.39%	9.05%	17.40%	133.33%
Hist. Cash Flow Growth (3-5 yrs)	19.94%	6.79%	8.55%	7.11%	9.98%	NA
Current Ratio	1.88	1.69	1.33	2.21	2.12	2.94
Debt/Capital	74.75%	40.41%	44.50%	63.29%	22.80%	12.55%
Net Margin	8.63%	-0.15%	10.13%	0.84%	5.15%	-37.71%
Return on Equity	35.42%	4.37%	14.39%	9.37%	14.93%	-29.33%
Sales/Assets	1.12	1.10	0.51	1.00	1.28	0.58
Proj. Sales Growth (F1/F0)	-32.08%	-17.59%	-1.51%	-24.62%	-20.00%	-32.87%
Momentum Score	D	-	-	F	B	C
Daily Price Chg	-2.20%	-0.41%	-0.04%	-2.88%	-0.37%	-2.39%
1 Week Price Chg	-3.19%	-0.55%	0.14%	-8.78%	0.09%	-10.19%
4 Week Price Chg	29.25%	7.87%	7.78%	11.44%	13.88%	-6.51%
12 Week Price Chg	34.42%	30.77%	17.48%	29.63%	34.06%	15.01%
52 Week Price Chg	17.87%	-1.86%	0.68%	-12.43%	5.77%	-40.93%
20 Day Average Volume	703,316	204,170	2,057,775	1,431,490	385,623	542,571
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-40.00%	6.57%	0.00%
(F1) EPS Est 4 week change	1.49%	0.00%	1.36%	-58.18%	15.36%	10.50%
(F1) EPS Est 12 week change	3.41%	-4.48%	1.57%	-69.20%	17.82%	8.66%
(Q1) EPS Est Mthly Chg	-7.14%	0.00%	0.54%	-48.86%	-9.76%	-20.69%

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	B
Growth Score	F
Momentum Score	D
VGM Score	D

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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