

Parker-Hannifin (PH)

\$140.32 (As of 03/13/20)

Price Target (6-12 Months): **\$147.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 01/21/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: B

Growth: C

Momentum: F

Summary

Parker-Hannifin expects strength in the aerospace end markets, unique Win Strategy and ongoing investments to drive its near-term revenues. Also, the company is likely to benefit from acquired assets (including CLARCOR, Exotic Metals Forming and LORD). In addition, it is on track to boost shareholder return over time. However, Parker-Hannifin expects business-realignment expenses of \$40 million for fiscal 2020. Also, foreign exchange headwind might have an adverse impact of 0.5% on its fiscal 2020 sales. Rise in debt levels can increase the company's financial obligations and hurt profitability. In the past three months, Parker-Hannifin's stock has underperformed the industry. Also, its earnings estimates have been lowered for the third and fourth quarters of fiscal 2020 in the past 60 days.

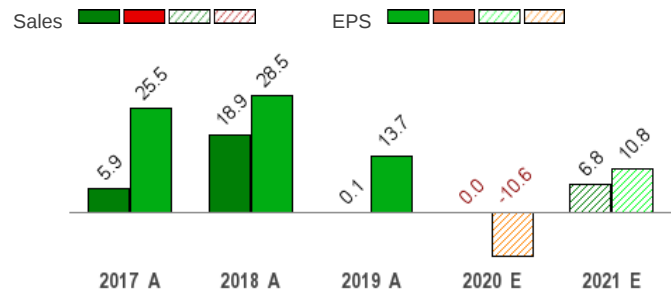
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$215.94 - \$123.01
20 Day Average Volume (sh)	1,577,672
Market Cap	\$18.0 B
YTD Price Change	-31.8%
Beta	1.47
Dividend / Div Yld	\$3.52 / 2.5%
Industry	Manufacturing - General Industrial
Zacks Industry Rank	Bottom 32% (171 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	10.9%
Last Sales Surprise	1.0%
EPS F1 Est- 4 week change	-0.1%
Expected Report Date	05/07/2020
Earnings ESP	0.3%
P/E TTM	11.9
P/E F1	13.3
PEG F1	1.5
P/S TTM	1.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	3,644 E	3,688 E	3,875 E	4,025 E	15,289 E
2020	3,335 A	3,498 A	3,673 E	3,802 E	14,315 E
2019	3,479 A	3,472 A	3,688 A	3,681 A	14,320 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.84 E	\$2.71 E	\$2.94 E	\$3.40 E	\$11.73 E
2020	\$2.76 A	\$2.54 A	\$2.43 E	\$2.84 E	\$10.59 E
2019	\$2.84 A	\$2.51 A	\$3.17 A	\$3.31 A	\$11.85 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 03/13/2020. The reports text is as of 03/16/2020.

Overview

Parker-Hannifin Corporation is a global diversified manufacturer of motion & control technologies and systems. The company provides precision engineered solutions for a wide variety of mobile, industrial and aerospace markets.

Diversified Industrial Segment (79% of second-quarter fiscal 2020 sales): This segment is engaged in the production of a wide range of motion-control and fluid systems & components. The products offered by this segment are used in transportation, mobile construction, refrigeration and air conditioning, agriculture and other markets.

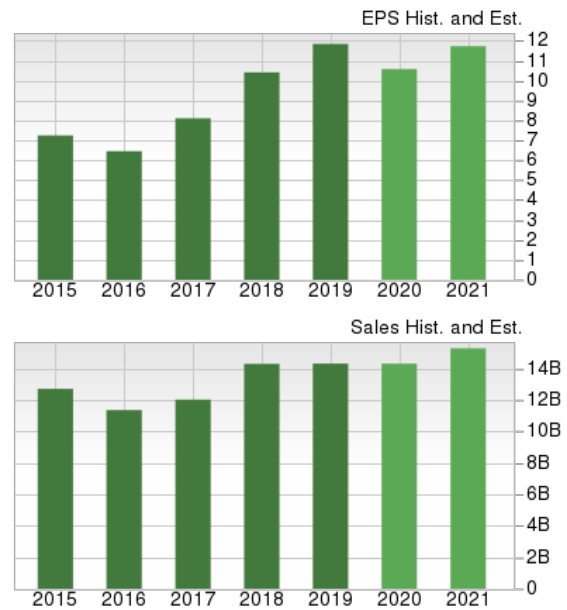
The segment sells its products through two main channels, namely, original equipment manufacturers (OEMs) and extensive distribution network to smaller OEMs and the aftermarket.

Products offered include sealing devices (dynamic and static); filters, systems and instruments to monitor and remove contaminants from fuel, air, oil, water and other liquids and gases; fluid connectors that control, transmit and contain fluid; hydraulic components and systems for builders and users of industrial and mobile machinery and equipment; and high-quality flow control solutions.

Aerospace Systems (21%): This segment supervises the designing and manufacturing of products and also provides aftermarket support for a broad range of aerospace products including commercial, business jet, military and general aviation aircraft and missile.

Products offered include control actuation systems & components, fluid metering, delivery & atomization devices, fuel systems & components, pneumatic control components, hydraulic systems & components and lubrication components among others.

The segment's products and services are offered to OEM and maintenance, repair and overhaul (MRO) customers throughout the world. Notably, the products are marketed by field sales employees and are sold to manufacturers as well as end customers.



Reasons To Buy:

- ▲ Parker-Hannifin reported better-than-expected revenues in second-quarter fiscal 2020, with the top line beating the Zacks Consensus Estimate by 1%. Also, the top line recorded growth of 0.7% year over year. Organic revenues for the company's Aerospace Systems segment improved 1.3% on the back of growth in military OEM and commercial aftermarket end markets. Robust backlog at the company's Aerospace Systems segment, which increased 55.4% at the end of fiscal second quarter, is likely to boost its top-line performance in the quarters ahead. Also, continued strength in end markets like marine, lawn and turf as well as recovery in mining and semiconductor end-markets, is likely to supplement the company's top-line performance. Moreover, benefits of its unique Win Strategy and ongoing investments are also expected to support the company's revenue growth.
- ▲ Parker-Hannifin intends to finance new growth-based investments, acquire businesses and boost shareholders' remuneration with increased liquidity. The company's CLARCOR acquisition (March 2017) is likely to bring in synergy savings worth roughly \$160 million in fiscal 2020. Also, in September 2019, it completed the acquisition of Exotic Metals Forming Company. Exotic Metals' unique products and proprietary manufacturing capabilities have been enhancing Parker-Hannifin's aerospace products and solutions. Moreover, the company's buyout of LORD Corporation (completed in October 2019) will enhance its engineered materials product and solutions offerings. Notably, in second-quarter fiscal 2020, these buyouts together contributed 38.9% to sales of the Aerospace Systems segment. Notably, the company believes that both these buyouts will continue to be accretive to organic growth and margins. Notably, it expects to achieve synergy savings of \$18 million from LORD and Exotic buyouts for fiscal 2020. As a matter of fact, the company believes the acquisitions will have a contribution of 6.9% to total sales for fiscal 2020.
- ▲ Parker-Hannifin is steadily improving its cash position. In the last five fiscal years (2015-2019), the company's cash flow from operations increased 5.9% (CAGR). Notably, in the first half of fiscal 2020, Parker-Hannifin's cash flow from operations was up a whopping 52.7% on a year-over-year basis. In addition, the company remains highly committed toward increasing wealth of its shareholders through dividend payouts. In this regard, it increased the quarterly dividend rate by 16% or 12 cents per share to 88 cents in April 2019. On an annualized basis, the dividend increased to \$3.52 from \$3.04 per share.

Strong backlog level, CLARCOR buyout benefits and ongoing Win Strategy are likely to drive Parker-Hannifin's near-term bottom-line results.

Reasons To Sell:

- ▼ In the past three months, Parker-Hannifin's shares have moved down 31.1% compared with the industry's decline of 20.9%. The company's realignment plan might prove beneficial over the long run, but will affect its near-term financials. For instance, in the first and second quarters of fiscal 2020, business realignment expenses hurt the company's adjusted earnings by 4 cents and 8 cents per share, respectively. As a matter of fact, for fiscal 2020, Parker-Hannifin expects to incur business realignment expenses of \$40 million. In addition, analysts have become increasingly bearish on the company over the past 60 days. Consequently, the Zacks Consensus Estimate for third-quarter fiscal 2020 earnings has trended down from \$2.71 to \$2.43 on seven downward estimate revisions against none upward. Further, the consensus estimate for fourth-quarter fiscal 2020 earnings has trended down from \$2.93 to \$2.84 over the same time frame.
- ▼ Parker-Hannifin's long-term debt in the last five fiscal years (2015-2019) increased 19.1% (CAGR). At the end of second-quarter fiscal 2020, the company's long-term debt was about \$8,141.2 million, up a whopping 89.2% on a year-over-year basis. Also, net interest expenses in the quarter were about \$82.9 million, up 74.5%. Moreover, we find the company more leveraged than the industry. The stock's long-term debt-to-capital ratio is 56.2%, higher than the industry's ratio of 50.9%. We believe that a highly leveraged balance sheet can inflate its financial obligations and hurt profitability.
- ▼ Parker-Hannifin intends to boost its revenues and profitability on the back of overseas business expansion. However, this exposes the company to several political, economic and environmental headwinds. For instance, a stronger U.S. dollar is currently weighing over the company's international revenues. Notably, adverse foreign currency translation impact had hurt Parker-Hannifin's fiscal first and second quarter revenues by 1.5% and 0.4%, respectively, on a year-over-year basis. As a matter of fact, for fiscal 2020, adverse foreign currency translation is likely to affect the company's top line by 0.5%.

Foreign exchange headwinds, high debt level and realignment expenses might weigh on Parker-Hannifin's results in the quarters ahead.

Last Earnings Report

Parker-Hannifin's Q2 Earnings & Revenues Top Estimates

Parker-Hannifin reported better-than-expected results for second-quarter fiscal 2020 (ended December 2019), wherein both earnings and revenues beat estimates.

Earnings/Revenues

Quarterly adjusted earnings came in at \$2.54 per share, up 1.2% year over year from \$2.51. Also, the bottom line outpaced the Zacks Consensus Estimate of \$2.29.

Revenues for the fiscal second quarter were about \$3,498 million, up 0.7% year over year. Moreover, the top line beat the consensus estimate of \$3,464 million.

Segmental Breakup

North American segment's revenues came in at \$1,615.9 million, down 1% year over year.

International's top-line figure declined 6.3% to \$1,147.1 million.

Aerospace Systems generated revenues of \$735 million, up 19.3%.

Costs/Margins

Cost of sales in the fiscal second quarter was \$2,682.8 million, up 3.1% year over year. Selling, general and administrative expenses were \$491.1 million, up from \$397.3 million. Adjusted operating margin was 15.8%, down 80 basis points.

Balance Sheet/Cash Flow

Exiting the fiscal second quarter, Parker-Hannifin had cash and cash equivalents of \$948.4 million, down from \$3,219.8 million recorded on Jun 30, 2019. At the end of the reported quarter, long-term debt was \$8,141.2 million compared with \$6,520.8 million as of Jun 30, 2019.

In first six months of fiscal 2020, the company generated about \$826 million cash from operating activities, up from \$541 million in the first six months of fiscal 2019.

Outlook

Parker-Hannifin intends to boost its near-term revenues and profitability on the back of its Win Strategy. The company revised earnings view for fiscal 2020 to \$10.25-\$10.85 from \$10.10-\$10.90 per share.

Quarter Ending **12/2019**

Report Date	Jan 30, 2020
Sales Surprise	0.99%
EPS Surprise	10.92%
Quarterly EPS	2.54
Annual EPS (TTM)	11.78

Recent News

On **Mar 12, 2020**, Parker-Hannifin discussed initiatives to grow organically, transforming the business, the Win Strategy 3.0, capital allocation policy and targets for fiscal 2023 (ending June 2023).

As noted, the company is poised to gain from lower costs (achieved through restructuring actions), streamlined organization structure (with 84 divisions versus 126 previously) and the Win Strategy 3.0 (implemented in fiscal 2019 — ended June 2019).

It is worth noting here that the Win Strategy 3.0 comprises four goals — including engaged people, customer experience, profitable growth and financial performance.

Also, it added that its healthy balance sheet and cash positions helped in making acquisitions. Notably, the CLARCOR acquisition in March 2017 will likely yield revenue synergies of \$100 million and cost benefits of \$160 million by fiscal 2020 (ending June 2020). Also, Exotic Metals Forming Company, acquired in September 2019, will likely result in cost gains of \$13 million by the end of fiscal 2023. The buyout of LORD Corporation in October 2019 will likely generate cost synergies of \$125 million by fiscal 2023 end.

Parker-Hannifin also communicated that its adjusted earnings will exclude expenses (intangible asset amortization) related to buyouts beginning fiscal 2021 (ending June 2021).

By fiscal 2023, Parker-Hannifin predicts revenue growth of 150 basis points (bps) greater than Global Industrial Production Index (GIPI). Both adjusted segment operating margin, and adjusted earnings before interest, tax, depreciation and amortization (EBITDA) are estimated to be 21%. Free cash flow is predicted to be \$2.3 billion, while adjusted earnings per share are anticipated to be \$16.90.

From fiscal 2019 to 2023, the company anticipates using \$16.5 billion capital for dividend payments of \$2.5 billion, capital expenditure of \$1.5 billion, share buyback of \$1 billion and debt reduction of \$3.9 billion. Also, it allocated \$2.2 billion for acquisitions and other purposes. Notably, \$5.4 billion was used for the Exotic and LORD buyouts. Gross debt to EBITDA is expected to reach 2.0x in fiscal 2023 from 2.8x in fiscal 2019.

On **Mar 6, 2020**, Parker-Hannifin paid out a quarterly cash dividend of 88 cents per share to shareholders of record as of Feb 7, 2020.

On **Jan 13, 2020**, Parker-Hannifin's Precision Fluidics division announced the launch of its latest Ultra Low Carryover Valve, a miniature liquid solenoid valve.

On **Jan 3, 2020**, Parker-Hannifin's business division, Electronic Controls, announced the launch of version 2.0 of its software tool suite for the PHD family of displays for mobile equipment.

On **Dec 20, 2019**, Parker-Hannifin's business division, Parker HVAC Filtration, unveiled two new filtration products, Parker Pur Ag SlimBox Filter and Parker Pur Ag V-Bank Filter, particularly for the agriculture industry.

Valuation

Parker-Hannifin shares declined 31.8% and 19.4% in the year to date period and over the trailing 12-months, respectively. Stocks in the Zacks sub-industry are down 21.5%, while the Zacks Industrial Products sector decreased 24.3% in the year-to-date period. Over the past year, the Zacks sub-industry and the sector decreased 12% and 19.7%, respectively.

The S&P 500 Index has moved down 15.8% year to date and 5.3% in the past year.

The stock is currently trading at 12.3X forward 12-month earnings per share, which compares to 16.98X for the Zacks sub-industry, 13.89X for the Zacks sector and 15.74X for the S&P 500 index.

Over the past five years, the stock has traded as high as 20.71X and as low as 11.45X, with a 5-year median of 15.94X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$147 price target reflects 12.92X forward 12-month earnings per share.

The table below shows summary valuation data for PH.

Valuation Multiples - PH					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	12.3	16.98	13.89	15.74
	5-Year High	20.71	23.5	19.89	19.34

P/E F12M	5-Year High	29.77	23.9	19.99	19.34
	5-Year Low	11.45	15.6	12.6	15.18
	5-Year Median	15.94	19.39	16.43	17.42
	Current	10.2	10.84	15.58	12.34
EV/EBITDA F12M	5-Year High	12.79	13.95	18.2	14.18
	5-Year Low	7.61	8.2	10.68	9.08
	5-Year Median	9.87	11.03	14.09	10.82
	Current	1.67	2.57	2.8	3.04
EV/Sales F12M	5-Year High	2.32	3.26	3.15	3.51
	5-Year Low	1.11	1.81	1.76	2.3
	5-Year Median	1.7	2.58	2.3	2.8

As of 03/13/2020

Industry Analysis Zacks Industry Rank: Bottom 32% (171 out of 253)



Top Peers

Donaldson Company, Inc. (DCI)	Neutral
Danaher Corporation (DHR)	Neutral
Emerson Electric Co. (EMR)	Neutral
Eaton Corporation, PLC (ETN)	Neutral
Honeywell International Inc. (HON)	Neutral
Gates Industrial Corporation PLC (GTES)	Underperform
Triumph Group, Inc. (TGI)	Underperform
United Technologies Corporation (UTX)	Underperform

Industry Comparison Industry: Manufacturing - General Industrial				Industry Peers		
	PH Neutral	X Industry	S&P 500	DCI Neutral	DHR Neutral	ETN Neutral
VGM Score	C	-	-	C	D	B
Market Cap	18.01 B	1.12 B	19.05 B	5.57 B	98.44 B	35.37 B
# of Analysts	8	4	13	6	7	10
Dividend Yield	2.51%	0.00%	2.31%	1.91%	0.48%	3.41%
Value Score	B	-	-	D	D	C
Cash/Price	0.05	0.07	0.05	0.04	0.19	0.02
EV/EBITDA	9.79	9.27	11.57	12.61	22.08	11.57
PEG Ratio	1.28	1.96	1.68	2.65	2.33	1.59
Price/Book (P/B)	2.84	1.81	2.56	5.92	3.54	2.19
Price/Cash Flow (P/CF)	9.01	8.42	10.18	15.19	22.75	10.82
P/E (F1)	11.70	13.81	14.94	20.74	26.08	14.87
Price/Sales (P/S)	1.27	0.98	2.02	2.01	4.94	1.65
Earnings Yield	7.55%	6.98%	6.67%	4.82%	3.83%	6.72%
Debt/Equity	1.28	0.51	0.70	0.69	0.75	0.51
Cash Flow (\$/share)	15.57	2.24	7.01	2.89	6.21	7.91
Growth Score	C	-	-	B	C	B
Hist. EPS Growth (3-5 yrs)	15.94%	7.61%	10.85%	10.06%	2.72%	6.55%
Proj. EPS Growth (F1/F0)	-10.68%	4.15%	5.99%	-4.15%	22.66%	1.48%
Curr. Cash Flow Growth	6.37%	4.08%	6.15%	8.18%	1.84%	0.36%
Hist. Cash Flow Growth (3-5 yrs)	7.55%	4.53%	8.52%	2.27%	5.87%	2.58%
Current Ratio	1.38	2.01	1.24	2.25	5.19	1.70
Debt/Capital	56.21%	33.99%	42.57%	41.12%	41.54%	33.56%
Net Margin	9.63%	6.24%	11.64%	9.47%	15.09%	10.34%
Return on Equity	25.18%	11.10%	16.74%	30.72%	11.50%	14.75%
Sales/Assets	0.77	0.77	0.54	1.25	0.35	0.67
Proj. Sales Growth (F1/F0)	-0.03%	0.00%	3.54%	-5.45%	6.78%	-5.18%
Momentum Score	F	-	-	F	F	D
Daily Price Chg	7.61%	3.02%	8.21%	9.14%	9.70%	12.70%
1 Week Price Chg	-10.71%	-1.94%	-0.67%	1.75%	2.66%	2.26%
4 Week Price Chg	-34.13%	-28.35%	-22.67%	-16.59%	-13.48%	-16.84%
12 Week Price Chg	-31.97%	-23.33%	-20.46%	-22.89%	-6.02%	-9.21%
52 Week Price Chg	-17.45%	-22.82%	-10.79%	-9.83%	10.37%	5.64%
20 Day Average Volume	1,577,672	56,962	3,061,271	654,867	3,473,255	3,943,944
(F1) EPS Est 1 week change	-0.09%	0.00%	0.00%	-1.47%	-0.48%	0.00%
(F1) EPS Est 4 week change	-0.09%	-0.03%	-0.32%	-6.13%	-0.48%	-0.14%
(F1) EPS Est 12 week change	-0.71%	-2.33%	-0.65%	-6.13%	-2.60%	-2.51%
(Q1) EPS Est Mthly Chg	-0.87%	-0.24%	-0.62%	-12.58%	-0.03%	-6.47%

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	C
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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