

Regal Beloit (RBC)

\$86.26 (As of 01/09/20)

Price Target (6-12 Months): **\$91.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 03/04/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:B

Value: A

Growth: C

Momentum: C

Summary

Regal Beloit is likely to benefit from acquisitions it made in the past. Nicotra Gebhardt, acquired in April 2018, has been strengthening the company's Commercial & Industrial Systems' operations. Business restructuring initiatives will help Regal Beloit to drive product innovation, organic growth and customer relationships. Moreover, it has started executing a simplification phase II program, which is likely to provide additional value creation opportunities. Also, rewarding shareholders handsomely works in Regal Beloit's favor. However, the stock has underperformed the industry in the past six months. The company faces divestment issues and forex woes. A highly-leveraged balance sheet can inflate its financial obligations. For 2019, the company expects organic sales to decline in the mid-single digit range.

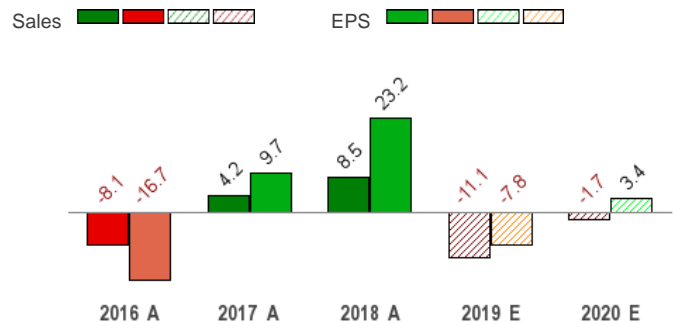
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$87.31 - \$67.74
20 Day Average Volume (sh)	191,571
Market Cap	\$3.5 B
YTD Price Change	0.8%
Beta	1.63
Dividend / Div Yld	\$1.20 / 1.4%
Industry	Manufacturing - Electronics
Zacks Industry Rank	Bottom 24% (192 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	1.5%
Last Sales Surprise	-6.4%
EPS F1 Est- 4 week change	-0.0%
Expected Report Date	02/03/2020
Earnings ESP	-0.2%
P/E TTM	15.1
P/E F1	15.1
PEG F1	1.5
P/S TTM	1.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	782 E	830 E	795 E	757 E	3,186 E
2019	854 A	874 A	772 A	742 E	3,242 E
2018	879 A	960 A	925 A	882 A	3,646 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$1.32 E	\$1.57 E	\$1.50 E	\$1.38 E	\$5.72 E
2019	\$1.43 A	\$1.52 A	\$1.35 A	\$1.24 E	\$5.53 E
2018	\$1.34 A	\$1.60 A	\$1.67 A	\$1.41 A	\$6.00 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 01/09/2020. The reports text is as of 01/10/2020.

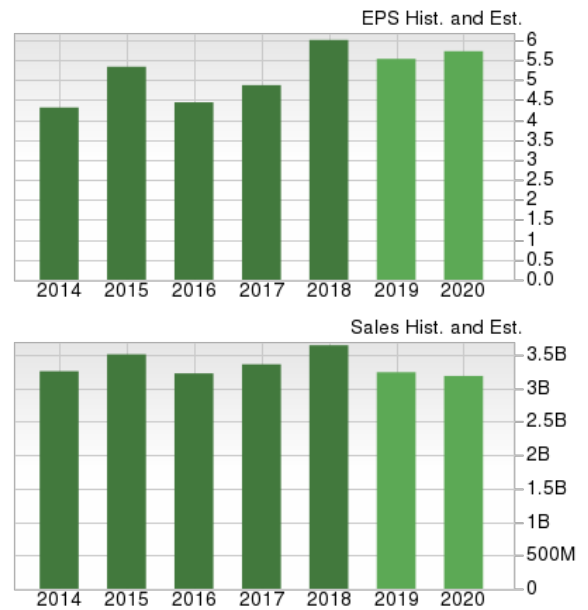
Overview

Headquartered in Beloit, WI, Regal Beloit Corporation is a leading manufacturer of electrical and mechanical motion control products. The company offers an array of electric motors, blowers, electric generators, transfer switches, gearboxes, power generation components and controls.

The company has manufacturing, sales and service facilities throughout the United States, Canada, Mexico, Europe, and Asia while it markets products to a diversified customer base across the globe — including OEMs, distributors and end users. Exiting 2018, the company had approximately 24,600 employees, including 5,320 in the United States, 11,355 in Mexico and 3,660 in China.

Regal Beloit currently reports revenues under three operating segments — Climate Solutions, Commercial and Industrial Systems, and Power Transmission Solutions. A brief discussion is provided below:

- **Climate Solutions** (29.9% of revenues generated in third-quarter 2019): The segment designs and manufactures small motors and controls for heating, ventilation, air conditioning (HVAC) applications for residential and light commercial industry; water heaters; and commercial refrigeration.
- **Commercial and Industrial Systems** (46.4%): The segment manufactures medium and large motors, alternators, motors, commercial & industrial equipment and air moving solutions. Products are mainly used in oil and gas systems, pool and spa, and commercial HVAC markets.
- **Power Transmission Solutions** (23.7%): The segment manufactures modular plastic belts, helical and worm gearing, belt and chain drives, mounted and unmounted bearings, conveying chains, couplings, hydraulic pump drives and other products. These products are mainly used in special machinery, beverage, energy, aerospace, bulk handling, metals and general industrial markets.



Reasons To Buy:

- ▲ Regal Beloit's management has implemented a radical change in the organizational structure by decentralizing operations in order to simplify decision making, improve speed of execution, boost operational efficiency and financial performance as well as better position the company for talent development. Also, the company believes that the reorganization into decentralized business units will allow its teams to leverage vertical knowledge and experience. This, in turn, will help the company to drive product innovation, organic growth and customer relationships. Moreover, it has started executing a simplification phase II program, which is likely to provide additional value creation opportunities. The reorganization and restructuring efforts led to 16% and 17% reduction in personnel, and selling, general and administrative costs, respectively, year over year, in the third quarter. As a matter of fact, Regal Beloit anticipates annual savings of \$15 million from the reorganization.
- ▲ Over time, Regal Beloit solidified its product portfolio and leveraged business opportunities through the addition of assets. Here, the buyout of Nicotra Gebhardt in April 2018 is worth mentioning. Since its acquisition, Nicotra Gebhardt has been strengthening Regal Beloit's Commercial & Industrial Systems segment. For instance, in the first nine months of 2019, acquired assets had a contribution of 1.2% to the company's sales growth. Moreover, Regal Beloit believes in divesting non-core businesses. In the first nine months of 2019, the company completed divestment of the highly engineered drives and control systems business (Regal Drive Technologies) and a vapor recovery business. As part of its restructuring plan, the company also announced its decision to close five additional plants, which will generate an annual savings of \$17 million, most of which is likely to come through 2020. These divestments will allow Regal Beloit to focus more on its core businesses.
- ▲ Regal Beloit remains committed toward rewarding shareholders handsomely through dividend payments and share buybacks. In the third quarter of 2019, the company repurchased shares worth \$94.2 million. Also, dividend payments amounted to \$12.6 million in the quarter. The quarterly dividend rate currently stands at 30 cents per share (hike of 7% was announced in April 2019). It's worth mentioning here that Regal Beloit approved a \$250-million share buyback program in October 2019. It noted that the new authorization replaces the earlier programs. We believe that further share buybacks by the company will help in improving the bottom line.

Business restructuring and simplification initiatives are likely to drive Regal Beloit. Also, its policy of rewarding shareholders handsomely works in its favor.

Reasons To Sell:

- ▼ In the past six months, Regal Beloit's shares have returned 9.3% compared with the industry's increase of 20.9%. In third-quarter 2019, the company's bottom line declined 13.5% year over year on weak sales performance and a fall in margins. For 2019, the company lowered adjusted earnings projection to \$5.45-\$5.55 per share from the previously stated \$5.50-\$5.80. The mid-point of the revised projection reflects a decline of 2.7% from the earlier mid-point. Also, the consensus mark for the company's earnings declined 0.8% for the fourth quarter of 2019 in the past 60 days.
- ▼ In the third quarter of 2019, Regal Beloit's top-line performance was weak. Sales lagged estimates by 6.4% and decreased 16.5% on a year-over-year basis. Organic sales declined 9.6% due to weakness in Climate Solutions, Commercial and Industrial Systems, and Power Transmission Solutions segments. The company anticipates that low order rates in residential HVAC and commercial refrigeration business are likely to adversely impact sales for the Climate Solutions in 2019. Also, weakness in commercial HVAC, North American pool pump businesses, lower industrial demand in China and uncertainties in global trade are likely to act as headwinds for the Commercial and Industrial Systems segment. Slowdown in North American industrial markets, coupled with weakness in beverage, oil & gas, and agriculture end markets are likely to affect the company's Power Transmission Solutions segment. For 2019, the company expects its organic sales to decline in mid-single digits compared with a low to mid-single-digit fall predicted earlier.
- ▼ Regal Beloit had a highly leveraged balance sheet. In the last five years (2014-2018), the company's long-term debt jumped 15.9% (CAGR), with long-term debt of \$1,200.3 million at the end of the third quarter of 2019. Net interest expenses in the quarter were \$13.5 million. We believe that further issuances of long-term debts will make the company more leveraged and can also inflate its financial obligations, hurting profitability. Also, international businesses exposed Regal Beloit to risks arising from unfavorable movements in foreign currencies and geopolitical issues. In second and third quarter of 2019, negative foreign exchange impact lowered sales by 1.5% and 0.7%, respectively. Persistence of forex woes might be concerning. Moreover, the company believes in making acquisitions to expand businesses, which, in turn, consumes significant resources and exposes it to integration risks. Divestments are done in the best interest of shareholders. However, business divestment may hurt near-term results. For instance, adverse impact of divested businesses adversely impacted the company's second- and third-quarter 2019 sales by 5.3% and 6.2%, respectively.

Weak organic sales prospects, a highly leveraged balance sheet and exposure to forex woes headwinds might hurt Regal Beloit's performance in the quarters ahead.

Last Earnings Report

Regal Beloit Beats Q3 Earnings Estimates, Lowers View

Regal Beloit delivered better-than-expected results for the third quarter of 2019, with earnings surpassing estimates by 1.5%. The company reported impressive results after its earnings lagged estimates by 6.75% in the second quarter of 2019.

Adjusted earnings in the reported quarter were \$1.35 per share, surpassing the Zacks Consensus Estimate of \$1.33. However, the bottom line declined 13.5% from the year-ago quarter's \$1.56 on weak sales performance and a fall in margins.

Quarter Ending **09/2019**

Report Date	Nov 04, 2019
Sales Surprise	-6.44%
EPS Surprise	1.50%
Quarterly EPS	1.35
Annual EPS (TTM)	5.71

Core Sales, Divestments and Forex Woes

In the reported quarter, Regal Beloit's net sales were \$772.3 million, declining 16.5% year over year. Organic sales in the quarter fell 9.6%, while forex woes and divestments had adverse impacts of 0.7% and 6.2%, respectively.

Further, the top line lagged the Zacks Consensus Estimate of \$825.4 million by 6.4%.

Excluding the impact of divested businesses, the company's adjusted net sales in the reported quarter were \$771.4 million, down 10.4% year over year.

Regal Beloit's reports results under three segments — Climate Solutions, Commercial and Industrial Systems, and Power Transmission Solutions. The quarterly segmental results are briefly discussed below:

Revenues from **Climate Solutions** totaled \$230.9 million, declining 9.6% year over year. It represented 29.9% of net sales. The results were adversely impacted by an organic sales decline of 4.8%, forex woes of 0.2% and divestiture impact of 4.6%. Notably, organic performance suffered from mild weather, headwinds related to residential HVAC, OEM destocking, weak commercial refrigeration business and other issues.

Commercial and **Industrial Systems'** revenues, representing 46.4% of net sales, were \$358.6 million, down 22.4% year over year. Organic sales in the reported quarter declined 12.7%, while divestments resulted in an adverse impact of 8.6%. Also, forex woes lowered sales by 1.1%.

Organic sales in the quarter suffered from weakness in the commercial HVAC market and industrial demand in China. Also, issues related to the pool pump market in North America and unfavorable timings of power generation projects played spoilsport.

Power Transmission Solutions' revenues, representing 23.7% of net sales, were \$182.8 million, down 12% year over year. Organic sales dipped 9.3% due to weakness in beverage, oil & gas, and agriculture end markets, partially offset by favorable business in the renewable energy market. Forex woes and divestments had adverse impacts of 0.6% and 2.1%, respectively.

Margin Picture

In the reported quarter, Regal Beloit's cost of sales declined 16.5% year over year to \$570.4 million. It represented 73.9% of net sales versus 73.8% recorded in the year-ago quarter. Gross margin declined 10 basis points (bps) to 26.1%. Operating expenses of \$129.1 million dipped 16.7% year over year and represented 16.7% of net sales in the quarter.

Adjusted operating profit was \$81.3 million, down 18.5% year over year, while margin declined 110 bps to 10.5%. Interest expenses in the quarter were down 1.5% year over year to \$13.5 million.

Adjusted effective tax rate in the quarter was 16.3% versus 20.2% in the year-ago quarter.

Balance Sheet and Cash Flow

Exiting the third quarter of 2019, Regal Beloit had cash and cash equivalents of \$293 million, reflecting 0.6% growth from \$291.3 million recorded in the last reported quarter. Long-term debt declined 1.8% sequentially to \$1,200.3 million.

In the third quarter, Regal Beloit generated net cash of \$140.6 million from operating activities, reflecting year-over-year growth of 32.6%. The company increased capital investment for purchasing property, plant and equipment by 12.8% over the year-ago figure to \$21.1 million. Free cash flow was \$119.5 million in the quarter versus \$87.3 million in the year-ago quarter.

Shareholder-Friendly Policies

During the third quarter of 2019, the company paid out dividends totaling \$12.6 million to shareholders and repurchased shares worth \$94.2 million.

Outlook

For 2019, the company lowered its adjusted earnings guidance to \$5.45-\$5.55 per share from previously stated \$5.50-\$5.80. The mid-point of the revised projection reflects a decline of 2.7% from the earlier mid-point. The company believes that prevailing headwinds — a slowdown in Asia, uncertainties in global trade, an industrial slowdown in the

United States and excess channel inventories — will affect its performance. Cost-out activities will be advantageous.

Organic sales are predicted to decline in mid-single digits versus a low to mid-single-digit fall mentioned earlier. Interest expenses (net) are predicted to be \$49 million.

Capital expenditure is predicted to be \$90 million and free cash flow is likely to be more than 115% of adjusted net income (marking an increase

from the previously stated figure). Adjusted effective tax rate will likely be 19.5%.

Recent News

Dividend

On **Jan 10, 2020**, Regal Beloit paid a quarterly cash dividend of 30 cents per share to shareholders of record as on Dec 27, 2019.

Share Buyback Program

On **Oct 25, 2019**, Regal Beloit's board of directors approved a \$250-million share buyback program. It noted that the new authorization replaces the earlier programs.

Valuation

Regal Beloit's shares have increased 20.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Industrial Products sector have moved up 23.3% and 17% over the past year.

The S&P 500 index has moved up 24.4% in the past year.

The stock is currently trading at 15.04x forward 12-month earnings per share, which compares to 20.39x for the Zacks sub-industry, 18.1x for the Zacks sector and 18.81x for the S&P 500 index.

Over the past five years, the stock has traded as high as 17.02x and as low as 8.78x, with a 5-year median of 12.97x. Our Neutral recommendation indicates that the stock will perform in line with the market. Our price target of \$91 reflects 15.79x forward 12-month earnings.

The table below shows summary valuation data for RBC.

Valuation Multiples - RBC					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	15.04	20.39	18.1	18.81
	5-Year High	17.02	20.39	19.9	19.34
	5-Year Low	8.78	13.14	12.59	15.17
	5-Year Median	12.97	17.03	16.54	17.44
EV/EBITDA F12M	Current	9.6	17.38	17.8	12.66
	5-Year High	9.69	25.03	18.2	12.66
	5-Year Low	6.57	9.9	10.68	9.08
	5-Year Median	8.33	13.36	13.99	10.78
EV/Sales F12M	Current	1.41	2.86	3.14	3.26
	5-Year High	1.47	2.86	3.14	3.37
	5-Year Low	0.94	1.52	1.76	2.3
	5-Year Median	1.25	2.06	2.28	2.78

As of 01/09/2020

Industry Analysis Zacks Industry Rank: Bottom 24% (192 out of 254)



Top Peers

ABB Ltd (ABB)	Neutral
Cummins Inc. (CMI)	Neutral
Nidec Corp. (NJDCY)	Neutral
Panasonic Corp. (PCRFY)	Neutral
Rexnord Corporation (RXN)	Neutral
Timken Company (The) (TKR)	Neutral
Altra Industrial Motion Corp. (AIMC)	Underperform
II-VI Incorporated (IIVI)	Underperform

Industry Comparison Industry: Manufacturing - Electronics				Industry Peers		
	RBC Neutral	X Industry	S&P 500	ABB Neutral	AIMC Underperform	RXN Neutral
VGM Score	B	-	-	C	B	B
Market Cap	3.53 B	2.27 B	23.94 B	51.68 B	2.35 B	3.47 B
# of Analysts	3	4	13	1	2	6
Dividend Yield	1.39%	0.00%	1.78%	2.03%	1.87%	0.00%
Value Score	A	-	-	C	C	A
Cash/Price	0.08	0.09	0.04	0.06	0.07	0.09
EV/EBITDA	9.18	11.62	13.97	17.30	24.48	10.93
PEG Ratio	1.51	1.88	2.03	3.77	NA	1.78
Price/Book (P/B)	1.55	2.27	3.33	3.77	1.26	2.62
Price/Cash Flow (P/CF)	9.16	13.16	13.73	13.77	12.91	10.67
P/E (F1)	15.13	18.75	18.79	23.35	13.63	16.81
Price/Sales (P/S)	1.04	1.83	2.64	1.83	1.26	1.69
Earnings Yield	6.63%	4.75%	5.32%	4.26%	7.32%	5.96%
Debt/Equity	0.54	0.27	0.72	0.62	0.87	0.95
Cash Flow (\$/share)	9.41	1.83	6.94	1.76	2.82	3.07
Growth Score	C	-	-	D	A	B
Hist. EPS Growth (3-5 yrs)	6.08%	5.47%	10.56%	3.70%	13.39%	4.86%
Proj. EPS Growth (F1/F0)	3.46%	7.94%	7.49%	12.50%	-6.30%	5.23%
Curr. Cash Flow Growth	14.06%	12.53%	14.83%	7.17%	84.71%	34.59%
Hist. Cash Flow Growth (3-5 yrs)	4.47%	3.18%	9.00%	-1.95%	19.13%	5.48%
Current Ratio	2.83	2.16	1.23	1.36	2.09	2.94
Debt/Capital	35.03%	24.28%	42.99%	38.35%	46.59%	48.60%
Net Margin	7.62%	6.86%	11.08%	5.06%	4.56%	8.56%
Return on Equity	10.14%	10.17%	17.16%	19.16%	9.83%	19.40%
Sales/Assets	0.73	0.88	0.55	0.63	0.43	0.63
Proj. Sales Growth (F1/F0)	-1.71%	0.62%	4.20%	-0.73%	-3.71%	0.66%
Momentum Score	C	-	-	B	D	F
Daily Price Chg	0.64%	-0.43%	0.53%	-0.70%	0.36%	0.49%
1 Week Price Chg	0.39%	0.36%	-0.30%	0.29%	1.84%	0.34%
4 Week Price Chg	1.91%	1.12%	1.92%	2.33%	2.76%	0.40%
12 Week Price Chg	18.29%	16.83%	6.54%	27.41%	28.74%	19.50%
52 Week Price Chg	19.26%	20.63%	22.58%	22.01%	27.35%	32.19%
20 Day Average Volume	191,571	185,823	1,580,816	1,762,601	291,081	619,595
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.98%	0.00%	0.00%
(F1) EPS Est 4 week change	-0.03%	0.00%	0.00%	0.98%	-0.19%	-0.34%
(F1) EPS Est 12 week change	-5.24%	-2.26%	-0.50%	1.14%	-1.11%	-1.27%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	NA	NA	-0.78%

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	A
Growth Score	C
Momentum Score	C
VGM Score	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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