

Regal Beloit (RBC)

\$63.35 (As of 03/12/20)

Price Target (6-12 Months): **\$67.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 02/06/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:B

Value: A

Growth: B

Momentum: F

Summary

In the quarters ahead, Regal Beloit is likely to benefit from business restructuring initiatives, which will help to boost transparency, focus and accountability of its operations. Moreover, its robust liquidity position and shareholder-friendly policies add to its strength. In the past 60 days, the company's earnings estimates have been raised for 2020. However, the stock has underperformed the industry in the past year. For 2020, the company expects organic sales to be flat to modestly down year over year, with a decline expected in the first half and recovery in the second half. Also, Regal Beloit faces divestment issues. A highly leveraged balance sheet can inflate its financial obligations and hurt profitability. In addition, given its extensive geographic presence, its financials are subject to forex exchange headwinds.

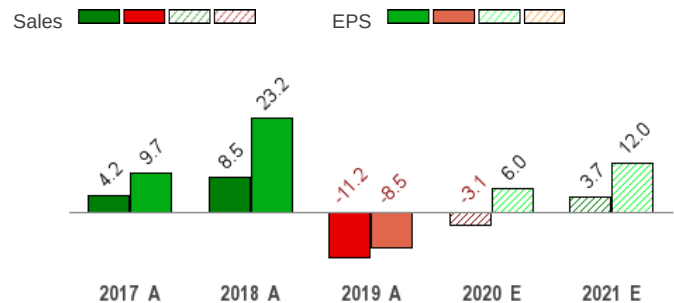
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$90.18 - \$63.35
20 Day Average Volume (sh)	352,789
Market Cap	\$2.6 B
YTD Price Change	-26.0%
Beta	1.43
Dividend / Div Yld	\$1.20 / 1.9%
Industry	Manufacturing - Electronics
Zacks Industry Rank	Bottom 38% (156 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	0.8%
Last Sales Surprise	-0.5%
EPS F1 Est- 4 week change	0.4%
Expected Report Date	05/04/2020
Earnings ESP	-0.5%
P/E TTM	11.4
P/E F1	10.9
PEG F1	1.1
P/S TTM	0.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					3,255 E
2020	764 E	826 E	787 E	761 E	3,138 E
2019	854 A	874 A	772 A	738 A	3,238 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$6.52 E
2020	\$1.25 E	\$1.55 E	\$1.49 E	\$1.51 E	\$5.82 E
2019	\$1.43 A	\$1.52 A	\$1.35 A	\$1.25 A	\$5.49 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 03/12/2020. The reports text is as of 03/13/2020.

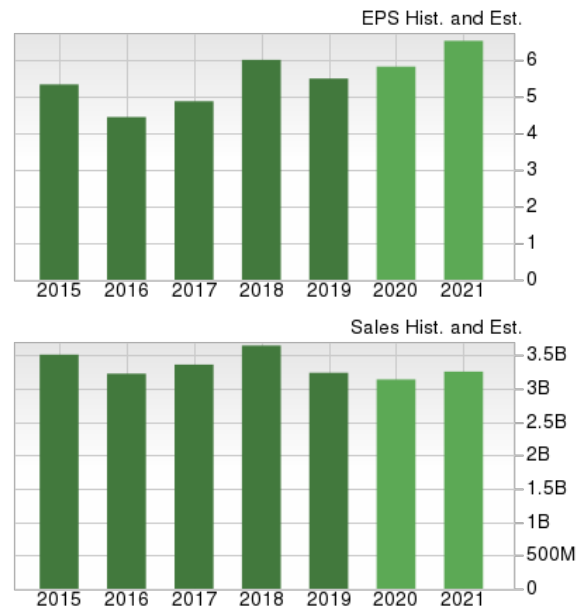
Overview

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.

In December 2019, Regal Beloit restructured its business into four segments to improve transparency, focus and accountability. Currently, the company reports operations under these segments — Climate Solutions, Commercial Systems, Industrial Systems, and Power Transmission Solutions. Details on these segments are provided below:

- **Climate Solutions** (28% of revenues generated in fourth-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 Systems** (27.4%): The segment manufactures medium motors, commercial & industrial equipment and air moving solutions. Products are mainly used in water pumps, pool and spa, and commercial HVAC markets.
- **Industrial Systems** (18.6): The segment is engaged in manufacturing large motors, alternators, automatic transfer switches and switchgear solutions. These products are primarily used in general industrial equipment, agriculture, oil and gas, data center and power generation markets.
- **Power Transmission Solutions** (26%): 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, and better position the company for talent development. Also, the company believes that its business restructuring move (December 2019) will improve transparency, focus and accountability, particularly for its Commercial Systems and Industrial Systems segments. Its simplification and footprint consolidation program has been providing additional value creation opportunities. As a matter of fact, Regal Beloit anticipates annual savings of more than \$38 million from the reorganization, restructuring and footprint consolidation program.
- ▲ Regal Beloit's robust liquidity position adds to its strength. In the last three years (2017-2019), the company's cash flow from operations increased 11.9% (CAGR). Notably, in the fourth quarter of 2019, the company's cash flow from operations as well as cash and cash equivalents were up 12.6% and 33.3%, respectively, on a year-over-year basis. In addition, analysts have become increasingly bullish about Regal Beloit over the past 60 days. The company's earnings estimates for 2020 have been raised from \$5.72 to \$5.82 on four upward estimate revisions versus one downward.
- ▲ Regal Beloit remains committed toward rewarding shareholders handsomely through dividend payments and share buybacks. In the fourth quarter of 2019, the company repurchased shares worth \$15 million. Also, dividend payments amounted to \$12.3 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, it has a policy of rewarding shareholders handsomely.

Reasons To Sell:

- ▼ In the past year, Regal Beloit's shares have dipped 22.4% compared with the industry's decline of 20.3%. In fourth-quarter 2019, the company's bottom line declined 4.6% year over year on weak sales performance and a fall in margins. In the fourth quarter, Regal Beloit's top-line performance was weak. Sales lagged estimates by 0.5% and decreased 16.3% on a year-over-year basis. Organic sales declined 9.3% due to weakness in Climate Solutions, Commercial Systems, Industrial Systems, and Power Transmission Solutions segments. The company expects low order rates in residential HVAC business to adversely impact sales for the Climate Solutions in the quarters ahead. Persistent weakness in North American pool pump business is likely to act as headwinds for the Commercial Systems segment. Soft demand from industrial motors market in North America and continued weak industrial demand in China remain concerns for the company's Industrial Systems segment. Slowdown in both upstream and downstream oil and gas end markets, North American industrial markets, coupled with softness in beverage, oil & gas, end markets might affect the company's Power Transmission Solutions segment. For 2020, the company expects organic sales to be flat to modestly down year over year, with a decline expected in the first half and recovery in the second half.
- ▼ Regal Beloit had a highly leveraged balance sheet. In the last three years (2017-2019), the company's long-term debt jumped 3% (CAGR), with long-term debt of \$1,136.9 million at the end of the fourth quarter of 2019. Net interest expenses in the quarter were \$12.5 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 third and fourth quarters of 2019, negative foreign exchange impact lowered sales by 0.7% and 0.5%, respectively. Persistence of forex woes might be concerning.
- ▼ Regal Beloit 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 third- quarter and fourth-quarter sales by 6.2% and 6.5%, 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 Q4 Earnings Estimates, Ups View

Regal Beloit reported lackluster fourth-quarter 2019 results due to declining income and revenues. However, the bottom line surpassed estimates by 0.8%. The company reported relatively weak results after its earnings surpassed estimates by 1.5% in the third quarter of 2019.

Adjusted earnings were \$1.25 per share, surpassing the Zacks Consensus Estimate of \$1.24. However, the bottom line declined 4.6% from the year-ago quarter's \$1.31 on weak sales and falling margins.

Adjusted earnings in 2019 were \$5.49 per share, down 2.7% from \$5.64 in 2018. The decline was primarily attributable to lower revenues.

Quarter Ending **12/2019**

Report Date	Feb 03, 2020
Sales Surprise	-0.50%
EPS Surprise	0.81%
Quarterly EPS	1.25
Annual EPS (TTM)	5.55

Core Sales, Divestments and Forex Woes

In the reported quarter, Regal Beloit's net sales were \$738.2 million, declining 16.3% year over year. Organic sales fell 9.3%, while forex woes and divestments had adverse impact of 0.5% and 6.5%, respectively.

In 2019, Regal Beloit's net sales were \$3,238 million, declining 11.2% year over year. Organic sales fell 5.7%, while forex woes and divestments had adverse impact of 1.1% and 5.3%, respectively.

Further, the top line lagged the Zacks Consensus Estimate of \$742 million by 0.5%.

Excluding the impact of divested businesses, the company's adjusted net sales in the reported quarter were \$738 million, down 9.8% year over year. Its full-year adjusted net sales were \$3,185.2 million, down 5.8%.

Per the latest reporting structure, Regal Beloit's reports results under four segments — Commercial Systems, Industrial Systems, Climate Solutions and Power Transmission Solutions. The quarterly segmental results are briefly discussed below:

Commercial Systems' revenues, representing 27.4% of net sales, were \$202 million, down 26.1% year over year. Organic sales in the reported quarter declined 10.4%, while divestments resulted in an adverse impact of 15.1%. Also, forex woes affected sales by 0.6%.

Organic sales suffered from weakness in North American general industry along with continued inventory reduction in the pool pump market in North America. Also, the effect of 80/20 account pruning played spoilsport.

Industrial Systems' revenues, representing 18.7% of net sales, were \$138 million, down 15.6% year over year. Organic sales declined 14.2%, while divestments and forex woes resulted in an adverse impact of 0.7%.

Decline in organic sales was primarily attributable to trade uncertainties in North America and China, and delays in power generation project due to end market overcapacity along with the aftermath of 80/20 account pruning. Also, downturn of oil and gas sectors played spoilsport.

Revenues from **Climate Solutions** totaled \$206.4 million, down 11.1% year over year. It represented 28% of net sales. Results were adversely impacted by an organic sales decline of 6.5%, forex woes of 0.2% and divestiture impact of 4.4%. Organic performance suffered from mild weather, headwinds related to residential HVAC, OEM destocking and 80/20 account pruning. However, the weak performance was partially offset by increasing demand in Asia-Pacific.

Power Transmission Solutions' revenues, representing 26% of net sales, were \$191.8 million, down 9.9% year over year. Organic sales dipped 7.2% due to weakness in the industrial distribution channel, backed by soft performance in upstream and midstream oil & gas sectors. However, the decline was partially offset by robust demand of renewable energy. Forex woes and divestments had adverse impacts of 0.4% and 2.3%, respectively.

Margin Picture

In the reported quarter, Regal Beloit's cost of sales declined 14.6% year over year to \$548 million. It represented 74.2% of net sales, up from 72.8%. Gross profit declined from \$239.7 million to \$190.2 million with respective margins of 27.2% and 25.8%. Operating expenses of \$128.5 million dipped 14.3% and represented 17.4% of net sales in the quarter.

Adjusted operating profit was \$77.5 million, down 11.1% year over year, while margin declined 10.7% to 10.5%. Interest expenses in the quarter were down 12.6% to \$12.5 million.

Adjusted effective tax rate in the quarter was 22.2% compared with 21% in the year-ago quarter.

Balance Sheet and Cash Flow

Exiting the fourth quarter, Regal Beloit had cash and cash equivalents of \$331.4 million, up 33.3% from \$248.6 million recorded at the end of 2018. Long-term debt declined 13% to \$1,136.9 million from the year-ago quarter.

In 2019, Regal Beloit generated net cash of \$137.3 million from operating activities, reflecting year-over-year growth of 22.2%. The company decreased capital investment for purchasing property, plant and equipment by 18% over the year-ago figure to \$15.1 million. Free cash flow was \$122.2 million in the reported quarter, up from \$94 million.

Shareholder Friendly Policies

During the fourth quarter, the company paid out dividends totaling \$12.3 million to shareholders and repurchased shares worth \$15 million.

The company purchased 180,763 shares worth \$15 million in the fourth quarter while it purchased 2,194,545 shares worth \$165 million in 2019.

Outlook

For 2020, the company expects adjusted earnings to be in the range of \$5.65-\$6.05 per share, reflecting year-over-year growth of 6.6% at the mid-point. The company believes that consistent profitability from differentiated products and services with the current re-segmentation is likely to have positive impact on the performance. The 80/20 account pruning effect will be advantageous.

Recent News

Investor Day

On **Mar 3, 2020**, Regal Beloit hosted its Investor Day. It discussed its long-term expectations as well as 2020 projections.

For 2020, the company maintained its adjusted earnings at \$5.65-\$6.05 per share. A close watch is being kept on the impacts of the coronavirus outbreak and short-cycle trends. Organic sales will likely be flat to modestly down year over year in 2020, with a decline expected in the first half and recovery in the second half. Free cash flow will likely be more than 100% of net income.

From 2020 to 2022, the company believes that organic sales will grow 2-3%, while total revenues will increase 1-2%. Also, expansion in adjusted operating margin will likely be 250-300 basis points, while adjusted earnings per share will likely grow 8-10% (CAGR). Free cash flow conversion will probably be more than 100%. Improvement in return on invested capital (ROIC) will likely be 250-300 basis points.

Dividend

On **Jan 27, 2020**, Regal Beloit's board of directors approved payment of a quarterly cash dividend of 30 cents per share to shareholders of record as on Mar 27, 2020. The payment will be made on Apr 9, 2020.

Valuation

Regal Beloit's have decreased 26% and 22.4% in the year to date period and over the trailing 12-month period, respectively. Stocks in the Zacks sub-industry have moved down 30.1%, while the Zacks Industrial Products sector has declined 30.9% in the year-to-date period. Over the past year, the Zacks sub-industry and the sector are down 20.3% and 25.5%, respectively.

The S&P 500 Index has moved down 23% in the year-to-date period and 12.5% in the past year.

The stock is currently trading at 10.71x forward 12-month earnings per share, which compares to 13.85x for the Zacks sub-industry, 12.95x for the Zacks sector and 14.38x for the S&P 500 index.

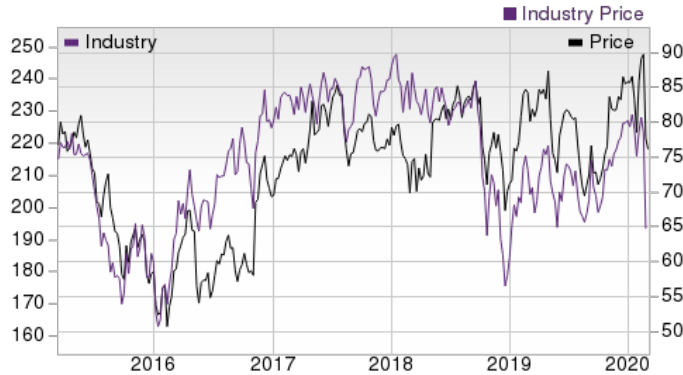
Over the past five years, the stock has traded as high as 17.02x and as low as 8.78x, with a 5-year median of 12.96x. Our Neutral recommendation indicates that the stock will perform in line with the market. Our price target of \$67 reflects 11.25x forward 12-month earnings.

The table below shows summary valuation data for RBC.

Valuation Multiples - RBC					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	10.71	13.85	12.95	14.38
	5-Year High	17.02	20.28	19.89	19.34
	5-Year Low	8.78	13.14	12.6	14.38
	5-Year Median	12.96	17.05	16.43	17.42
EV/EBITDA F12M	Current	8.24	15.27	15.58	12.34
	5-Year High	9.69	25.03	18.2	14.18
	5-Year Low	6.66	9.9	10.68	9.08
	5-Year Median	8.4	13.68	14.09	10.82
EV/Sales F12M	Current	1.26	2.53	2.8	3.04
	5-Year High	1.47	2.87	3.15	3.51
	5-Year Low	0.98	1.52	1.76	2.3
	5-Year Median	1.26	2.09	2.29	2.8

As of 03/12/2020

Industry Analysis Zacks Industry Rank: Bottom 38% (156 out of 253)



Top Peers

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

Industry Comparison Industry: Manufacturing - Electronics				Industry Peers		
	RBC Neutral	X Industry	S&P 500	ABB Neutral	AIMC Underperform	RXN Neutral
VGM Score	B	-	-	B	B	B
Market Cap	2.58 B	1.83 B	17.38 B	35.98 B	1.15 B	2.67 B
# of Analysts	5	4	13	3	2	6
Dividend Yield	1.89%	0.00%	2.51%	2.92%	3.81%	1.46%
Value Score	A	-	-	B	C	B
Cash/Price	0.11	0.10	0.05	0.09	0.10	0.08
EV/EBITDA	6.99	8.37	10.90	12.72	7.24	8.80
PEG Ratio	1.09	1.41	1.54	2.68	NA	1.32
Price/Book (P/B)	1.09	1.51	2.35	2.57	0.60	1.95
Price/Cash Flow (P/CF)	7.08	9.49	9.60	9.98	3.62	7.15
P/E (F1)	10.88	13.69	13.98	16.61	6.98	11.07
Price/Sales (P/S)	0.80	1.30	1.89	1.29	0.63	1.30
Earnings Yield	9.19%	6.95%	7.07%	6.00%	14.35%	9.03%
Debt/Equity	0.50	0.32	0.70	0.48	0.83	0.84
Cash Flow (\$/share)	8.94	1.79	7.01	1.69	4.92	3.07
Growth Score	B	-	-	C	C	C
Hist. EPS Growth (3-5 yrs)	5.54%	6.27%	10.85%	3.57%	15.19%	6.27%
Proj. EPS Growth (F1/F0)	5.94%	4.84%	5.99%	-18.28%	-10.66%	7.03%
Curr. Cash Flow Growth	-9.82%	4.43%	6.15%	-3.96%	74.66%	34.59%
Hist. Cash Flow Growth (3-5 yrs)	1.95%	1.94%	8.52%	-2.99%	29.14%	5.48%
Current Ratio	2.87	2.16	1.24	1.31	1.96	2.79
Debt/Capital	33.29%	23.63%	42.57%	32.63%	45.25%	45.61%
Net Margin	7.38%	6.86%	11.64%	5.14%	6.94%	9.66%
Return on Equity	9.69%	9.67%	16.74%	18.71%	9.77%	18.82%
Sales/Assets	0.71	0.88	0.54	0.62	0.42	0.63
Proj. Sales Growth (F1/F0)	-3.09%	0.00%	3.54%	-0.74%	-4.32%	0.60%
Momentum Score	F	-	-	B	A	C
Daily Price Chg	-12.60%	-10.02%	-10.03%	-10.62%	-16.48%	-18.06%
1 Week Price Chg	-2.04%	-1.54%	-0.67%	-2.87%	-15.47%	-4.32%
4 Week Price Chg	-29.20%	-29.66%	-28.22%	-30.80%	-52.30%	-38.20%
12 Week Price Chg	-25.79%	-27.95%	-25.63%	-30.11%	-49.13%	-33.21%
52 Week Price Chg	-22.38%	-19.91%	-16.72%	-12.25%	-43.46%	-18.63%
20 Day Average Volume	352,789	242,548	3,061,271	2,585,191	412,763	1,003,645
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.38%	-0.14%	-0.32%	0.33%	-4.49%	-0.08%
(F1) EPS Est 12 week change	1.68%	-3.77%	-0.65%	-1.14%	-4.66%	1.37%
(Q1) EPS Est Mthly Chg	-4.93%	-2.79%	-0.62%	NA	NA	-0.65%

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	B
Momentum Score	F
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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